FILE COPY

No. 250

In the Supreme Court of the United States

October Term, 1959

The United States of America, appellant

v.

Manufacturers National Bank of Detroit, a National Banking Association, as Executor of the Last Will and Testament of Clifford E. Longley, deceased

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MICHIGAN

JURISDICTIONAL STATEMENT

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CITATIONS

518214—59——1

In the Supreme Court of the United States

OCTOBER TERM, 1959

No. ——

THE UNITED STATES OF AMERICA, APPELLANT

v.

MANUFACTURERS NATIONAL BANK OF DETROIT, A NATIONAL BANKING ASSOCIATION, AS EXECUTOR OF THE LAST WILL AND TESTAMENT OF CLIFFORD B. LONGLEY, DECEASED

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MICHIGAN

JURISDICTIONAL STATEMENT

OPINION BELOW

The opinion of the District Court (Appendix, *infra*, pp. 10–16) is not yet reported.

JURISDICTION

This suit was brought under the authority of 28 U.S.C. 1346, for the recovery of estate taxes paid. It was alleged in the complaint and the District Court held that the statute under which the tax was levied (Section 811(g) of the 1939 Internal Revenue Code, as amended by Section 404 of the Revenue Act of 1942, c. 619, 56 Stat. 798, *infra*, pp. 2–3) is unconstitutional in its application to this case. The

judgment of the District Court was entered on June 26, 1959 (Appendix, *infra*, p. 17), and the notice of appeal was filed on June 30, 1959. The jurisdiction of this Court to review the judgment on direct appeal is conferred by 28 U.S.C. 1252 and 2101. *Fernandez* v. *Wiener*, 326 U.S. 340; *Fleming* v. *Rhodes*, 331 U.S. 100.

STATUTES INVOLVED

The pertinent provisions of the Internal Revenue Code of 1939 (Section 811(g)), and the Revenue Act of 1942, c. 619, 56 Stat. 798 (Section 404), are as follows:

1. Internal Revenue Code of 1939:

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * *

(g) [as amended by Sec. 404(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Proceeds of Life Insurance.*—

(1) *Receivable by the executor.*—To the extent of the amount receivable by the executor as insurance under policies upon the life of the decedent.

(2) *Receivable by other beneficiaries.*—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in proportion that the amount so paid by the decedent bears

to the total premiums paid for the insurance, or (B) with respect to which the decedent possessed at ~~his death~~ any of the incidents of ownership, exercisable either alone or in conjunction with any other person. For the purposes of clause (A) of this paragraph, if the decedent transferred, by assignment or otherwise, a policy of insurance, the amount paid directly or indirectly by the decedent shall be reduced by an amount which bears the same ratio to the amount paid directly or indirectly by the decedent as the consideration in money or money's worth received by the decedent for the transfer bears to the value of the policy at the time of the transfer. For the purposes of clause (B) of this paragraph, the term "incident of ownership" does not include a reversionary interest.

* * * * *

(26 U.S.C. 1952 ed., 811.)

2. Revenue Act of 1942, c. 619, 56 Stat. 798:

SEC. 404. PROCEEDS OF LIFE INSURANCE.

* * * * *

(c) *Decedents to Which Amendments Applicable.*—The amendments made by subsection (a) shall be applicable only to estates of decedents dying after the date of the enactment of this Act [October 21, 1942]; but in determining the proportion of the premiums or other consideration paid directly or indirectly by the decedent (but not the total premiums paid) the amount so paid by the decedent on or before January 10, 1941, shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policy.

QUESTION PRESENTED

Whether an estate tax provision (Section 811(g) of the Internal Revenue Code of 1939, as amended by Section 404 of the Revenue Act of 1942) requiring, in the computation of gross estate, the inclusion of proceeds of insurance on the life of the decedent to the extent the insurance has been purchased with premiums paid by the decedent, regardless of other aspects of ownership, is unconstitutional as an unapportioned direct tax or as a deprivation of property without due process of law.

STATEMENT

The material facts as stipulated and found by the District Court (Appendix, *infra*, pp. 10–16) may be summarized as follows:

The decedent died testate on July 15, 1954, and the taxpayer is the executor of his estate. The executor filed an estate tax return for the decedent's estate and included the proceeds of four policies of insurance on the life of the decedent in the total amount of $126,193.21. All of these policies had been taken out by the decedent prior to December 18, 1936, when he assigned and transferred all of the incidents of ownership in the policies to his wife, Harriet.

The decedent paid all the premiums on the policies from the time they were taken out until the time of his death. After the decedent died, the proceeds were retained and held by the insurance company for the benefit of his wife and children pursuant to the provisions of a settlement option plan that the wife selected.

In auditing the estate tax return, the Internal Revenue Service determined that only the proportion of the proceeds of these policies that the premiums paid by the decedent after January 10, 1941, bear to the total premiums paid should be included in the gross estate, reducing the amount includable in respect to these policies from $126,193.21 to $64,823.84, a reduction of $61,369.37; and a refund of the tax attributable to this adjustment was made to the estate. This resulted from an application of Section 811(g)(2)(A) of the 1939 Code, as amended by Section 404(a) of the Revenue Act of 1942, *supra*, p. 2–3, which was applicable to the estates of persons dying after October 21, 1942, the date of the enactment of the amendment. The Code, as amended, provided that proceeds of insurance on the life of a decedent receivable by beneficiaries other than the executor should be included in the gross estate for purposes of federal estate taxes to the extent that the insurance was purchased with premiums paid by the decedent, that amount to be determined on the basis of the proportion of the payments by the decedent to the total premiums for the insurance. However, in calculating premiums paid by a decedent, the amendment excluded payments made by a decedent on or before January 10, 1941 [1] if at no time after such date the decedent possessed an incident of ownership in the policy.

---

[1] This was the effective date of T.D. 5032, 1941-1 Cum. Bull. 427, which interpreted the statute (Section 811(g) of the 1939 Code, as it stood prior to the 1942 amendments) as providing that the payment of premiums alone should suffice to support the estate tax without regard to whether the decedent possessed any of the incidents of ownership in the policies. See I Paul, *Federal Estate and Gift Taxation* (1942 ed.),

* The taxpayer filed a claim for a further refund on the ground that Section 811(g) of the 1939 Code, as amended, *supra*, pp. 2–3, was unconstitutional in its application to this case and therefore that none of the proceeds of the policies should have been included in the taxable estate. The claim was not allowed by the Commissioner of Internal Revenue and the taxpayer brought this action in the District Court. That court sustained the taxpayer's contentions, held the section unconstitutional, and gave judgment for the taxpayer.

THE QUESTION IS SUBSTANTIAL

The decision of the court below was entirely based on considerations of constitutionality. Neither in this case, nor the case from the Seventh Circuit on which it relies, nor the cases with which it is in conflict, does the issue turn upon a question of fact or of statutory construction. The case presents a direct conflict on a constitutional issue which should be resolved by this Court.

In deciding the case against the Government, the District Court adopted the reasoning in *Kohl* v. *United States*, 226 F. 2d 381 (C.A. 7). In that case the court took the view that, since the decedent did not own the policies at the time of his death, there was no transfer at that time and the tax must necessarily have been imposed upon ownership of the proceeds, and that such a tax was a direct tax on such proceeds without apportionment in violation of Article I, Section 9, of the Constitution.[2]

Section 10.13, p. 514; (1946 Supp.), Section 10.34, p. 351; *Colonial Trust Co.* v. *Kraemer*, 63 F. Supp. 866, 871–872 (D. Conn.).

[2] The Government did not petition for certiorari in the *Kohl* case because, after the decision of the Seventh Circuit, it was

The decision of the District Court in the present case is supported by *Kohl,* but is in conflict with *Estate of Loeb* v. *Commissioner,* 261 F. 2d 232 (C.A. 2), affirming 29 T.C. 22; *Schwarz* v. *United States,* 170 F. Supp. 2 (E.D. La.); *Colonial Trust Co.* v. *Kraemer,* 63 F. Supp. 866 (D. Conn.); *Estate of Baker* v. *Commissioner,* 30 T.C. 776.

While it is true that the present estate tax provision (Section 2042 of the Internal Revenue Code of 1954, 26 U.S.C. Supp. V, 2042) eliminates the premium-payment test, the change operates prospectively only with respect to the estates of decedents dying after August 16, 1954. In addition to the conflicts which have already developed involving courts in the Second, Fifth and Seventh Circuits, as well as the Tax Court, other cases under the old law have already arisen or are in the administrative stage, in the Fourth and Eighth Circuits. Some of these cases involve very substantial sums of money.

Moreover, in addition to the specific application of the court's reasoning to this particular provision of the 1939 Code, the basis of the opinion below is of fundamental importance to the imposition of the estate tax generally, and, in our opinion is in conflict with the principles adopted by this Court. The fundamental error in the position of the court below was its failure to recognize that there does not have to be a "transfer" at death in a strict and technical

decided that an appeal had erroneously been taken by the Government to the Court of Appeals from the adverse decision of the District Court and that appeal should properly have been direct to this Court, as in the present case.

sense to justify the estate tax (*Tyler* v. *United States*, 231 U.S. 497, 502–503); and since life insurance is by its nature closely related to a testamentary disposition, the proceeds of insurance on the decedent's life can be taxed where he has paid the premiums even though he retained none of the incidents of ownership. The situation is similar to one where a transfer is made in contemplation of death or with reserved right to revoke with the consent of a beneficiary. In such cases, it is settled that the transfer is taxable because it is a substitute for a testamentary disposition. *Milliken* v. *United States*, 283 U.S. 15; *Helvering* v. *City Bank Co.*, 296 U.S. 85.

Cases such as *United States* v. *Bess*, 357 U.S. 51, referred to by the District Court in its opinion (Appendix, *infra*, p. 12) have no bearing on estate taxes or the constitutional questions raised in the instant case. The Court held in the *Bess* case that proceeds of a life insurance policy are not the property of the insured for purposes of determining the transferee liability of insurance beneficiaries for income taxes of the insured; but that holding did not relate to estate taxes and does not touch upon the well-established principle that the estate tax is not limited to property owned by or passing directly from the decedent but also extends to "property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another." *Chase Nat. Bank* v. *United States*, 278 U.S. 327, 337.

In the circumstances, there is nothing arbitrary nor unreasonable about the tax in this case, and it does not violate the Fifth Amendment. *Burnet* v. *Wells*,

289 U.S. 670. Moreover, there is no adequate basis for any contention that the tax is objectionably retroactive. All of the premiums on which the instant tax was based were paid after January 10, 1941, the date of T.D. 5032, 1941-1 Cum. Bull. 427 (see footnote 1, *supra*, p. 5). Therefore, even before the 1942 amendment, the tax consequences of the payments were the same, cf. *Welch* v. *Henry*, 305 U.S. 134, 147; *Milliken* v. *United States*, 283 U.S. 15, 23. Moreover, the tax in the present case is supported by the fact that the beneficiaries did not come into possession of the insurance proceeds until the death of the decedent; and since the decedent did not die until July 1954, it cannot rightly be said that the tax was retroactively imposed. *United States* v. *Jacobs*, 306 U.S. 363, 366; *Fernandez* v. *Wiener*, 326 U.S. 340, 354-355.

CONCLUSION

For the reasons stated, it is respectfully submitted that probable jurisdiction should be noted.

J. LEE RANKIN,
Solicitor General.
ABBOTT M. SELLERS,
Acting Assistant Attorney General.
MYRON C. BAUM,
L. W. POST,
Attorneys.

AUGUST, 1959.

APPENDIX

United States District Court for the Eastern District of Michigan, Southern Division

[Caption omitted.]

Opinion

Plaintiff brings this suit to recover estate taxes paid by it as executor for the estate of Clifford B. Longley, who died July 15, 1954. The issue here is simply whether a section of the Internal Revenue Code of 1939, as amended, is unconstitutional as applied in this case. The identical question has been decided by several courts prior to this time, but there is a conflict in their decisions. It appears to us that there is no reconciliation possible and that we must reach a yes or no result. We shall proceed, therefore, to set forth the considerations which have led us to adopt as our own, the views set forth in the particular decision with which we concur.

At the outset, let us state that this case has been submitted to the Court for decision upon a stipulation of facts [1] and upon the briefs of the respective parties. The Court has had the benefit of thorough and well prepared briefs.

At the time of the death of the decedent herein, July 15, 1954, there was still in effect the 1939 Internal Revenue Code. Approximately a month later the 1954 Code went into effect, and the provision of the 1939 Code here under consideration was eliminated. Were the 1954 Code operative in the instant case, there would be no question but that the insurance proceeds here in dispute would not be subject to the estate tax.

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[1] Attached as appendix hereto.

The beneficiary of the insurance policies here was the owner thereof, by virtue of assignment dated December 18, 1936. The decedent retained no incident of ownership from that date on. He had paid all premiums prior to the assignment and continued to pay all subsequent thereto. The assignment instrument provides that the beneficiary (wife) had the right to change beneficiary, reinstatement, surrender options, dividend rights prior to maturity of policy, loans to pay premiums, settlement option, cash loans and receipt of proceeds as endowment. The situation of the decedent here with respect to his rights in the policy is the same as that of the decedent in these recent cases, namely,

> *Kohl* v. *U.S.* 226 F. (2d) 381 (7 Cir., 1955),
> *Loeb's Estate* v. *Commissioner,* 261 F. (2d) 232 (2 Cir., 1958),[2]
> *Schwarz* v. *U.S.* 170 F. Supp. 2 (E.D. La., 1959).

The language of the Internal Revenue Code of 1939, as amended, which is the focal point of the cases cited above and of this case, is set forth here:

> § 810. *Rate of Tax*
> A tax * * * shall be imposed upon the transfer of the net estate of every decedent * * *.
> § 811. *Gross estate*
> The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—
>
> * * * * *
>
> (g) Proceeds of life insurance * * *
> (1) *Receivable by the executor.*—To the extent of the amount receivable by the executor

[2] Affirming *Estate of Clarence H. Loeb*, 29 T.C. 22.

as insurance under policies upon the life of the decedent.

(2) *Receivable by other beneficiaries.*—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance, * * *.

In reaching our determination of this case we have considered the cases cited by counsel for the respective parties. We have also endeavored to seek guidance from opinions of the Supreme Court and of the Court of Appeals for the Sixth Circuit. We have been impelled toward resolving this case in favor of the plaintiff, on the basis of the reasoning found in *United States* v. *Bess*, 357 U.S. 51 (1958); *Tyson* v. *Commissioner*, 212 F. (2d) 16 (6 Cir., 1954); and *Stern* v. *Commissioner*, 242 F. (2d) 322 (6 Cir., 1957).[3] We are well aware that § 311 (a)(1), (f) of the Internal Revenue Code of 1939 involved in these 3 cases is different from § 811 and that a different concept may be involved—there the question of unpaid income taxes of a decedent is treated. However, the term *transfer* there has been considered as of paramount importance. In the instant case it is of paramount importance that insurance proceeds be deemed to constitute a *transfer* if the tax is to be upheld. Despite all the arguments that may be advanced against using a §311 case as authority for a § 811 case, this Court takes the view that logic as such does not vary from statute to statute or case to case. If 2 plus 2 equals 4 for one purpose, it

[3] Affirmed 1958, 357 U.S. 39.

equals it for all, absent a different semantic hypothesis. It is the logic found within the confines of the 3 opinions just cited—*Bess, Tyson, Stern*—that has brought us to the conclusion that no transfer of the property herein sought to be included in the estate of this decedent occurred at the time of his death. Therefore, to the extent that § 811(g)(2) is sought to be applied to the insurance proceeds herein, it is unconstitutional. We think that this conclusion is implicit in the holdings in the *Bess, Tyson* and *Stern* cases, *supra,* which cases we have used by way of analogy. We therefore adopt the reasoning in the *Kohl* case, *supra,* as our own.

A judgment may be presented accordingly.

Dated at Detroit, Michigan, this 1st day of June A.D. 1959.

THOMAS P. THORNTON,
United States District Judge.

In the United States District Court for the Eastern District of Michigan, Southern Division

[Caption omitted.]

Stipulation of Facts

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel, that the following facts may be taken as true and may be included by the court in its findings of fact, subject to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated.

1. Clifford B. Longley died testate on July 15, 1954, a resident of the City of Detroit, County of Wayne and State of Michigan. His will was duly admitted to probate by the Probate Court for Wayne County, Michigan, on the 27th day of August, 1954, and on the same date Manufacturers National Bank of

Detroit, a National Banking Association (the plaintiff in this cause) was appointed as executor of the estate of said Clifford B. Longley. It was duly qualified and is still acting as such executor.

2. The plaintiff as such executor on October 13, 1955, filed an Estate Tax Return on Treasury Form 706 on account of the estate of said decedent with the District Director of Internal Revenue at Detroit, Michigan, and paid the tax shown as due by said return, namely, $55,044.61.

3. The following policies of insurance on the life of said decedent, all issued by the Mutual Benefit Life Insurance Company of Newark, New Jersey, were included in "Schedule D-Insurance" of said return at the following values:

Item No.	Policy No.	Value as returned
5	1, 093, 763	$25, 120. 83
6	1, 302, 517	25, 171. 00
7	1, 302, 518	25, 548. 38
8	1, 552, 548	50, 353. 00
Total		126, 193. 21

Attached hereto and marked "Exhibit A" is a copy of said policy 1,093,763. Attached hereto and marked "Exhibit B" is a copy of said policy 1,302,517. Attached hereto and marked "Exhibit C" is a copy of said policy 1,302,518 and attached hereto and marked "Exhibit D" is a copy of said policy 1,552,548.

4. Under date of December 18, 1936, said decedent executed a document, a copy of which is hereto attached and marked "Exhibit E." Said document was received on January 2, 1937, by Johnston & Clark, the general agents in Detroit, Michigan, of said Mutual Benefit Life Insurance Company at that time. On or about January 4, 1937, said document was re-

ceived by the "Agreement Department" of the Mutual Benefit Life Insurance Company of Newark, New Jersey, and a copy of said document was endorsed on each of said policies.

5. Both before and after the execution of such document, and up to the date of his death, ~~said~~ decedent paid all premiums on said policies of insurance.

6. Under date of December 19, 1936, Harriet B. Longley, the wife of decedent mentioned in the said document of which Exhibit E is a copy, executed and delivered to the Insurance Company an instrument, copy of which is attached hereto and marked "Exhibit F." A copy of said document was endorsed on each of said policies, and the proceeds of said policies are now held pursuant to the provisions of said document and of said policies.

7. On audit of said return by the Internal Revenue Service, it was discovered that in determining the proportion to total premiums, of premiums paid directly or indirectly by said decedent, Clifford B. Longley, plaintiff had not excluded the premiums paid by decedent before January 10, 1941. The resulting adjustment by the Internal Revenue Service reduced the value of such policies of insurance deemed includible in the gross estate for purposes of the estate tax to the following amounts:

Item No.	Policy No.	Corrected Value
5	1,093,763	$10,646.87
6	1,302,517	12,279.19
7	1,302,518	11,823.64
8	1,552,548	30,074.14
Total		64,823.84

8. The adjustment referred to in paragraph 7, to-

gether with another adjustment, resulted in a net reduction of $56,388.82 in the adjusted gross estate of said decedent. This reduction resulted in an overassessment of $7,781.65 in the amount of the estate tax previously paid by plaintiff as executor on account of the estate of said decedent. Such overassessment, together with interest in the amount of $37.10, or a total of $7,818.75, was duly refunded plaintiff as such executor, on September 18, 1956.

9. On November 20, 1956, the plaintiff filed with the District Director of Internal Revenue at Detroit, Michigan, a claim for refund (Treasury Form 843) of estate taxes paid on behalf of the estate in the amount of $8,945.70, plus interest. A copy of such claim is attached as Exhibit B to the Complaint filed in this case. The Commissioner of Internal Revenue has not issued a statutory notice of disallowance of such claim for refund.

10. The amount of estate tax paid by plaintiff which is attributable to the inclusion in the gross estate of said decedent of the value of such policies of insurance as so reduced in paragraph 7 herein shall be determined by the joint mathematical computation of the parties immediately after the questions involved herein have been decided by this Court.

(S) Henry I. Armstrong, Jr.,
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United States Attorney,
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By (S) Elmer L. Pfeifle, Jr.,
ELMER L. PFEIFLE, JR.,
Asst. United States Attorney.

Dated AUGUST 20, 1958.

United States District Court
Eastern District of Michigan,
Southern Division

[Caption omitted.]

Judgment

At a session of said Court held in the Federal Building at Detroit, Michigan, on June 26, 1959.

Present: Honorable THOMAS P. THORNTON, United States District Judge.

The Court having considered the evidence and the arguments of counsel, and having entered its findings of fact and conclusions of law herein, it is in conformity therewith:

Ordered, That plaintiff have judgment against defendant for the principal amount of $8,945.70, with interest thereon at six percent according to law from October 15, 1955.

THOMAS P. THORNTON,
District Judge.

Approved as to form:
FRED W. KAESS,
United States Attorney.
By [S] Elmer L. Pfeifle, Jr.,
ELMER L. PFEIFLE, JR.,
Assistant United States Attorney.

U S GOVERNMENT PRINTING OFFICE 1959

FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

No. 350

THE UNITED STATES OF AMERICA,
Appellant,

vs.

MANUFACTURERS NATIONAL BANK OF DETROIT,
a National Banking Association, as Executor
of the Last Will and Testament of
Clifford B. Longley, Deceased,
Appellee

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MICHIGAN

MOTION TO DISMISS APPEAL OR TO AFFIRM JUDGMENT

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IN THE

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OCTOBER TERM, 1959

No. 350

THE UNITED STATES OF AMERICA,
Appellant,

vs.

MANUFACTURERS NATIONAL BANK OF DETROIT,
a National Banking Association, as Executor
of the Last Will and Testament of
Clifford B. Longley, Deceased,
Appellee

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MICHIGAN

MOTION TO DISMISS APPEAL OR TO AFFIRM JUDGMENT

The Appellee, pursaunt to Rule 16 of the Supreme Court, moves:

1. That the appeal taken by the United States of America from the judgment of the District Court of the United States for the Eastern District of Michigan entered on June 26, 1959, in the cause therein pending

wherein Appellee is plaintiff and Appellant is defendant, be dismissed for the reason that such appeal does not present a substantial federal question since the statutory enactment held unconstitutional by said District Court has since been repealed by Congress, and since the amount of the judgment from which this appeal is taken, is trifling.

2. Or, in the alternative, that said judgment be affirmed on the ground that it is manifest that the question sought to be presented by this appeal is unsubstantial having already been clearly and recently decided by this Court.

FACTS

The facts in this case are accurately set forth in the Jurisdictional Statement.

QUESTION PRESENTED

As to the question presented, I believe that th following is a more correct statement than that appearing on page 4 of the Jurisdictional Statement:

Can a tax be levied constitutionally upon the transfer of the assets constituting the estate of a decedent because of the existence of policies of insurance on his life though neither such policies nor their proceeds are in any way included in his estate?

Under Section 811(g)(2)(A) of the Internal Revenue Code of 1939 as amended (26 U. S. C. A. 1948 Ed. 811 (g)(2)(A), the proceeds of policies of insurance on the life of decedent were used for the purpose of increasing the estate tax on his estate, though neither the policies nor their proceeds were among the assets constituting his estate. It is the position of Appellee that this constitutes

a direct tax on the assets of the estate which is unconstitutional because unapportioned contrary to Article I Section 2 and Article I Section 9 of the Constitution and which constitutes a deprivation of property without due process of law contrary to the Fifth Amendment.

ARGUMENT

1. This appeal should be dismissed because no substantial federal question is presented by it.

As is pointed out on page 7 of the Jurisdictional Statement, Congress has repealed this unconstitutional section of the 1939 Code. The section of the Internal Revenue Code of 1954, which relates to estate taxes on life insurance, omits all reference to the taxation of transfers of the proceeds of policies of insurance on the life of a decedent simply because the decedent has paid the premiums. (I. R. C. 1954 Sec. 2042; 26 U. S. C. A. 2042). If this decedent had died a month later, the proceeds of these policies would not have been included in his estate. It may be that some old cases involving this repealed statute are still pending, but they cannot be numerous. Moreover, the amount of the judgment involved in this case ($8,945.70 plus interest) is, comparatively speaking, trifling.

2. In the alternative, if this appeal is not dismissed, the judgment of the District Court should summarily be affirmed.

This court has very recently held that the proceeds of policies of insurance on the life of a decedent form no part of his estate unless payable to his estate. *United States v. Bess*, 357 U. S. 51. In this case, the United

States sought to hold the widow of a deceased taxpayer liable for his income tax deficiencies. The widow had received the proceeds of policies on his life and the Government sought to hold her as a transferee under Section 311(a)(1) of the Internal Revenue Code of 1939. The decedent had retained the right to change beneficiaries and so on. The proceeds of the policies amounted to $63,576.95 and the cash surrender value to $3,362.53. It was held that the widow was not a transferee of the proceeds of the policies. This Court said (pp. 55-56):

> "It would be anomalous to view as 'property' subject to lien proceeds never within the insured's reach to enjoy, and which are reducible to possession by another only upon the insured's death when his right to change the beneficiary comes to an end."

In other words, the widow was not a transferee of the insurance proceeds.

The estate tax is a tax upon the *transfer* of assets. In the 1939 Code it was imposed by Section 810 (26 U. S. C. A. 1948 Ed. 810):

> "A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 812) shall be imposed upon the *transfer of the net estate* of every decedent citizen or resident of the United States * * *." (Emphasis supplied.)

Obviously under the authority of the Bess case there was no *transfer* of the proceeds of this insurance. This Court has held that in some cases, where a decedent has retained certain rights with respect to property which are less than full ownership, the *termination* of these rights at his death may be considered as a transfer for purposes of the estate tax. Thus in the Bess case *supra* the decedent had retained the right to change the beneficiaries of the

policies involved up to the time of his death. Accordingly, this Court held that the widow was a transferee of the surrender value of the policies ($3,362.53).

In our case, no rights with respect to the policies were transferred or terminated by the death of decedent. The transfer had been effected by a gift made years ago. Of course, this gift would have been subject to the gift tax if large enough. Let it be admitted for the sake of argument that Congress could impose an excise tax on the receipt of the proceeds of life insurance, the tax here involved is not such a tax. It is purely and simply a tax on the assets of the decedent, imposed by reason of the ownership of the estate assets, plus the existence, not the ownership or transfer, of certain policies of insurance. Since it is a tax based purely on the ownership of these assets it is a direct tax and it is unconstitutional because not apportioned.

CONCLUSION

It is respectfully submitted therefore that this appeal should be dismissed or that the judgment of the District Court should be affiremd.

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Detroit 26, Michigan.

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UNITED STATES OF AMERICA, APPELLANT

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MANUFACTURERS NATIONAL BANK OF DETROIT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MICHIGAN

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the District Court (R. 24–27) is reported at 175 F. Supp. 291.

JURISDICTION

This suit was brought under 28 U.S.C. 1346 for the recovery of estate taxes levied pursuant to a statute which, as applied in this case, was alleged to be unconstitutional. The judgment of the District Court holding the statute unconstitutional was entered on June 26, 1959. (R. 27.) The notice of appeal was filed on June 30, 1959 (R. 28–29), and probable jurisdiction was noted on November 9, 1959 (R. 30). The jurisdiction of this Court rests on 28 U.S.C. 1252 and 2101.

QUESTION PRESENTED

Section 811(g)(2)(A) of the 1939 Internal Revenue Code requires inclusion in the decedent's gross estate, for purposes of the federal estate tax, of proceeds of insurance on the life of the decedent to the extent the insurance was purchased with premiums paid by him, regardless of whether he retained any incidents of ownership of the insurance policy.

The question presented is whether this provision, when applied to a portion of the proceeds of insurance policies that the decedent had assigned to the beneficiary, is unconstitutional either (1) as an unapportioned direct tax, or (2) as contravening the due process clause of the Fifth Amendment.

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of the United States Constitution (Article I, Sections 2, 8 and 9, and the Fifth Amendment); the Internal Revenue Code of 1939 (Section 811(g)); the Revenue Act of 1942, c. 619, 56 Stat. 798 (Section 404(c)); and Treasury Regulations 105 (Section 81.27), are set forth in the Appendix, *infra*, pages 26–29.

STATEMENT

The material facts, as stipulated and as found by the District Court (R. 15–21, 24–25), are as follows:

The decedent died testate on July 15, 1954, and the taxpayer is the executor of his estate. The executor included in the estate tax return the proceeds of four insurance policies on the life of the decedent, payable to his wife, in the total amount of $126,193.21.

These policies had been taken out by the decedent prior to December 18, 1936, when he assigned and transferred all the incidents of ownership in the policies to his wife. (R. 15–16, 18–19, 24–25.)

The decedent paid the premiums on the policies from the time they were taken out until he died. After his death, the proceeds were retained and held by the insurance company for the benefit of his wife and children pursuant to the provisions of a settlement option plan that the wife had selected. (R. 16–17, 20–21, 25.)

In the estate tax return, the executor treated the entire proceeds of the four policies as part of the gross estate. In auditing the return, the Internal Revenue Service determined that, under Section 811(g)(2)(A) of the Internal Revenue Code of 1939 (*infra*, p. 27) (the Code provision governing the application of the estate tax to such insurance policies), only the proportion of the proceeds of these policies that the premiums paid by the decedent after January 10, 1941, bear to the total premiums paid should be included in the gross estate. This adjustment reduced the amount includable from $126,193.21 to $64,834.84, and the amount of tax attributable to this adjustment ($7,781.65) was refunded. (R. 9, 17.)

Taxpayer then filed a claim for a further refund covering the tax on the portion of the proceeds attributable to the premiums paid by decedent after January 10, 1941. It contended that since the decedent had previously parted with all interest in the policies, the imposition of an estate tax on any portion

of the proceeds would be unconstitutional as a direct tax that was not apportioned, in violation of Article I, Sections 2 and 9 of the Constitution. (R. 9–10.) The Commissioner of Internal Revenue did not allow the claim, and the taxpayer then filed an action in the district court for refund, based upon the same theory of unconstitutionality. (R. 4, 17.) Taxpayer subsequently amended its complaint to allege that the tax was also unconstitutional under the due process clause of the Fifth Amendment "because it is retroactive and discriminatory in its operation * * *." (R. 22–23.)

The district court sustained taxpayer's contention that, as applied to the proceeds of insurance policies that the decedent had assigned to the beneficiary, Section 811(g)(2) is unconstitutional. It held (R. 25–26) that since the decedent "retained no incident of ownership" in the policies after their assignment to his wife in 1936, "no transfer of the property herein sought to be included in the estate of this decedent occurred at the time of his death." The court stated (R. 26) that it "adopt[ed] the reasoning" in *Kohl* v. *United States*, 226 F. 2d 381 (C.A. 7) "as our own." [1]

SUMMARY OF ARGUMENT

Section 811(g)(2)(A) of the Internal Revenue Code of 1939, as amended by the Revenue Act of

[1] In *Kohl*, the court held that where a decedent had assigned all interest in insurance policies to his children, there was no transfer at the time of his death; that the estate tax on the proceeds, therefore, must necessarily have been imposed upon the ownership of the proceeds; and that such a tax was a direct unapportioned tax upon such proceeds. The court further held that the tax was retroactive, in violation of the Fifth Amendment.

1942, provides that proceeds of insurance on the life of the decedent receivable by beneficiaries other than the executor, shall be included in the gross estate for purposes of the federal estate tax to the extent of the amount purchased with premiums paid directly or indirectly by the decedent, *i.e.*, in the proportion that the amount so paid by the decedent bears to the total premiums paid. The 1942 Act further provides that, if the decedent possessed no incidents of ownership in the policy after January 10, 1941, the premiums paid by him before that date are to be excluded in determining the portion of the proceeds for which he paid the premiums. In the instant case, the decedent, who died in 1954, had assigned all his interest in the policies to his wife in 1936; the Commissioner, therefore, assessed the estate tax solely on that portion of the proceeds for which the decedent had paid premiums after January 10, 1941.

The district court held that, as thus applied, the statute is unconstitutional. It reasoned that since the decedent had parted with all incidents of ownership in the policies, there was no "transfer" of any property interest of his in the policies upon death; and that the tax, therefore, was a direct tax upon the proceeds of the policies themselves that was invalid because not apportioned. The district court apparently also held that the statute as applied contravened the due process clause of the Fifth Amendment.

A. 1. The estate tax may be constitutionally applied even though there is no direct "transfer", in

the strict sense, of property from the deceased to the beneficiaries upon death. More than 30 years ago, in *Chase Nat. Bank* v. *United States,* 278 U.S. 327, this Court rejected the contention that an estate tax on the proceeds of life insurance policies is a direct tax that must be apportioned. The Court held (p. 337) that "the privilege which may constitutionally be taxed, cannot be taken in such a restricted sense as to refer only to the passing of particular items of property directly from the decedent to the transferee. It must, we think, at least include the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another." This Court has reiterated this same basic concept that the estate tax may constitutionally be "laid upon the shifting at death of some of the incidents of property" (*Fernandez* v. *Wiener,* 326 U.S. 340, 361) in applying the tax in various situations where death caused a ripening of property rights, even though, in the strict sense, there was no "transfer" of property from the decedent to his beneficiaries.

In the instant case, the "practical effect" (*Whitney* v. *Tax Commission,* 309 U.S. 530, 539) of the death of the insured was the ripening of rights which had been merely inchoate. We submit that such a ripening of rights clearly was an appropriate occasion for the imposition of an estate tax. "Receipt in possession and enjoyment is as much a taxable occasion within the reach of the federal taxing power as the enjoyment of any other incident of property" (*Fernandez, supra,* p. 353). The fact that the insured previously

had parted with all incidents of ownership in the policies is immaterial to the constitutional question involved, namely, "whether the [insured's] death has brought into being or ripened for the survivor, property rights of such character as to make appropriate the imposition of a tax upon that result * * *" (*Tyler* v. *United States*, 281 U.S. 497, 503).

2. Further support for the constitutionality of the instant tax may be found in the cases sustaining the application of the estate tax to *inter vivos* transfers made in contemplation of, or intended to take effect at death. *E.g.*, *Milliken* v. *United States*, 283 U.S. 15. In those cases, the application of the estate tax has been sustained even though there was no transfer of property at death, on the theory that since the gift was a means of carrying out the donor's testamentary design, Congress was justified in treating it as the equivalent of a testamentary disposition for estate tax purposes. Since life insurance is similarly "inherently testamentary in character" (*Bailey* v. *United States*, 27 F. Supp. 617, 621 (Ct. Claims)), the same reasoning justifies treating the proceeds of insurance for which the insured paid the premiums as part of his gross estate for estate tax purposes.

B. As applied in the instant case, Section 811(g)(2)(A) does not offend the due process clause of the Fifth Amendment.

1. The tax was not applied retroactively. Although the insured assigned all the policies to his wife in 1936, prior to the effective date of the 1942 amendment imposing the tax on the basis of premiums paid, he continued to pay the premiums until his death in

1954. The tax was applied only to that portion of the proceeds that was attributable to premiums that he paid after January 10, 1941, the effective date of the Treasury Regulation which subjected insurance proceeds to the estate tax on the basis of premiums paid by the decedent. With respect to premiums paid after that date the decedent was on notice that the insurance attributable thereto would be treated as part of his gross estate. Moreover, since the tax was here imposed on the theory that the beneficiary's interest in the proceeds ripened upon the death of the insured—long after the statute was enacted—the tax cannot be said to have been retroactively applied in any realistic sense. *United States* v. *Jacobs,* 306 U.S. 363, 366–367.

2. The tax is neither unreasonable nor arbitrary. As indicated, the death of the insured ripened property rights in the beneficiary which made imposition of a tax appropriate; moreover, insurance is sufficiently akin to testamentary dispositions to justify treating its proceeds as part of the decedent's gross estate. The tax fairly reflects the extent to which the decedent was responsible for creating the fund.

ARGUMENT

SECTION 811 (g) (2) (A) OF THE INTERNAL REVENUE CODE OF 1939 IS CONSTITUTIONAL WHEN APPLIED TO IMPOSE AN ESTATE TAX UPON THE PROCEEDS OF LIFE INSURANCE POLICIES FOR WHICH THE DECEDENT HAS PAID THE PREMIUMS, EVEN THOUGH HE HAD PARTED WITH ALL INCIDENTS OF OWNERSHIP IN THE POLICIES

Section 811(g)(2)(A) of the 1939 Internal Revenue Code, as amended by Section 404(a) of the Reve-

nue Act of 1942, c. 619, 56 Stat. 798 (Appendix, *infra*, pp. 27–28), provides that proceeds of insurance on the life of the decedent receivable by beneficiaries other than the executor shall be included in the gross estate for purposes of the federal estate tax to the extent of the amount purchased with premiums paid directly or indirectly by the decedent, *i.e.*, in the proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance. The 1942 Act further provides that if the decedent possessed no incidents of ownership in the policy after January 10, 1941, the premiums paid by him before that date are to be excluded in determining the portion of the proceeds for which he paid the premiums (Section 404(*c*), *infra*, p. 28).[2]

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[2] January 10, 1941 was the effective date of a Treasury Regulation (T.D. 5032, 1941-1 Cum. Bull. 427) which provided that, under Section 811(g) prior to the 1942 amendments, the proceeds of insurance were part of the gross estate to the extent that the decedent had paid the premiums thereon, whether or not he retained any incidents of ownership therein. Immediately prior thereto, the Regulations had imposed taxability only where the insured retained the incidents of ownership. The 1941 Regulation further provided that premiums paid by the decedent on or before its effective date were excluded if thereafter the decedent did not have any incidents of ownership in the policy. The 1942 amendments adopted this standard, and also provided, as an alternative basis for the tax, the incidents-of-ownership test.

Estate taxation of insurance proceeds was first specifically provided in the Revenue Act of 1918; the provision remained substantially unchanged until the 1942 amendments. During this period, however, the Treasury Regulation sometimes applied the payment-of-premiums test, sometimes the incidents-of-ownership test, and sometimes both. See *Estate of Ellis Baker*, 30 T.C. 776, 781–782; 1 Paul, *Federal Estate and Gift Taxation* (1942 ed.), § 10.13.

In the instant case, since the decedent had assigned all his interest in the policies to his wife in 1936, he had no incidents of ownership therein after January 10, 1941. Accordingly, the Commissioner, in determining the portion of the proceeds attributable to premiums paid by the decedent, included only premiums paid after the latter date.

The district court held that, as thus applied, the statute is unconstitutional as a direct tax that had not been apportioned. It reasoned that since prior to death the decedent had parted with all incidents of ownership in the policies, there was no "transfer" of any property interest of his in the policies upon death; and that the tax, therefore, was a direct tax upon the proceeds of the policies themselves, rather than an indirect tax upon the transfer of the decedent's interest therein.

It is well settled, however, that the estate tax may be constitutionally applied even though there is no technical "transfer" of property upon death. For the test of constitutionality is "not whether there has been, in the strict sense of that word, a 'transfer' of the property by the death of the decedent, or a receipt of it by right of succession, but whether the death has brought into being or ripened for the survivor, property rights of such character as to make appropriate the imposition of a tax upon that result (which Congress may call a transfer tax, a death duty or anything else it sees fit), to be measured, in whole or in part, by the value of such rights." *Tyler* v. *United States*, 281 U.S. 497, 503. As we shall show, the "inherent testamentary character" of life insurance (*Chase National Bank* v. *United States*, 116 F.

2d 625, 627 (C.A. 2), makes "appropriate the imposition of a tax," measured by the value of the proceeds attributable to the premiums paid by the decedent, with respect to the beneficiary's "property rights" that are "brought into being or ripened" by the death of the insured. We shall argue that, as applied in this case, Section 811(g)(2)(A) is not a direct tax on property, but a valid "excise tax * * * laid upon the shifting at death of some of the incidents of property" (*Fernandez* v. *Wiener,* 326 U.S. 340, 361). We shall further show that, as thus applied, the statute does not contravene the due process clause of the Fifth Amendment.

A. Section 811(g)(2)(A) is an indirect, not a direct, tax.

1. More than 30 years ago, in *Chase Nat. Bank* v. *United States,* 278 U.S. 327, this Court rejected the contention that an estate tax on the proceeds of life insurance policies is a direct tax upon such proceeds that must be apportioned.[3] It was there argued that

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[3] It has long been recognized that Congress has power to impose a tax on the transfer of an estate by death; and that such a tax is not a direct one, but a duty or excise, not requiring apportionment. *New York Trust Co.* v. *Eisner,* 256 U.S. 345, 349; *Greiner* v. *Lewellyn,* 258 U.S. 384, 387. In the *Greiner* case, this Court said (p. 387):

> That the Federal Government has power to tax the transmission of legacies was settled by *Knowlton* v. *Moore,* 178 U.S. 41; and that it has the power to tax the transfer of the net assets of a decedent's estate was settled by *New York Trust Co.* v. *Eisner,* 256 U.S. 345. The latter case has established also that the estate tax imposed by the Act of 1916, like the earlier legacy or succession tax, is a duty or excise, and not a direct tax like that on income from municipal bonds. *Pollock* v. *Farmers' Loan & Trust Co., supra.* * * *

the tax was a tax on property "because the beneficiaries' interests in the policies were not transferred to them from the decedent, but from the insurer, and hence there was nothing to which a transfer or privilege tax could apply" (p. 337). The Court stated (*ibid.*), however:

> Obviously, the word "transfer" in the statute, or the privilege which may constitutionally be taxed, cannot be taken in such a restricted sense as to refer only to the passing of particular items of property directly from the decedent to the transferee. It must, we think, at least include the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another. * * *

The Court further pointed out (p. 338) that "the real subject of the tax" is "the completion of [the] shifting of the economic benefits of property * * *."

The Court has reiterated this same basic concept that the estate tax may constitutionally be "laid upon the shifting at death of some of the incidents of property" (*Fernandez* v. *Wiener, supra*) in applying the tax in various situations where death caused a ripening of property rights, even though, in the strict sense of the word, there was no "transfer" of property from the decedent to his beneficiaries. See, *e.g., Fernandez, supra; Tyler* v. *United States*, 281 U.S. 497; *United States* v. *Jacobs*, 306 U.S. 363. As the Court emphasized in *Fernandez* (p. 352), "the power of Congress to impose death taxes is not limited to the taxation of transfers at death. It extends to the creation, exercise, acquisition, or relin-

quishment of any power or legal privilege which is incident to the ownership of property, and when any of these is occasioned by death, it may as readily be the subject of the federal tax as the transfer of the property at death." "[T]he emphasis in these cases [was] on the practical effect of death in bringing about a shift in economic interest, and the power of the legislature to fasten on that shift as the occasion for a tax" (*Whitney* v. *Tax Commission*, 309 U.S. 530, 539).

In the instant case, it is clear that the "practical effect" of the death of the insured was the ripening of rights in the beneficiary which had been merely inchoate. For prior to death the beneficiary had merely the incidents of ownership of the policies, such as the right to surrender them for cash, to pledge them as security, or to assign them. But it was only upon the death of the insured that the beneficiary received the full measure of what the policies were intended to provide, namely, the face amount of the insurance. We submit that the fruition of these rights was an appropriate occasion for the imposition of the estate tax. As this Court stated in *Fernandez* (p. 353):

> If the gift of property may be taxed, we cannot say that there is any want of constitutional power to tax the receipt of it, whether as the result of inheritance, *Stebbins* v. *Riley*, 268 U.S. 137, or otherwise, whatever name may be given to the tax, and even though the right to receive it, as distinguished from its actual receipt and possession at a future date, ante-

> dated the statute. Receipt in possession and enjoyment is as much a taxable occasion within the reach of the federal taxing power as the enjoyment of any other incident of property. * * *

In the circumstances, the fact that the decedent had parted with all incidents of ownership in the policies is immaterial to the constitutional question involved, namely, "whether the [insured's] death has brought into being or ripened for the survivor, property rights of such character as to make appropriate the imposition of a tax upon that result * * *" (*Tyler* v. *United States*, 281 U.S. 497, 503). As we have shown, this question must be answered affirmatively.

Although there may not have been any direct transfer of property from the insured to the beneficiary upon the former's death, the district court plainly erred in concluding (R. 26) that "no transfer of the property herein sought to be included in the estate of this decedent occurred at the time of his death." For the proceeds of the policies were transferred from the insurance company to the beneficiary upon the insured's death, and the estate tax may be imposed upon "the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another." *Chase Nat. Bank* v. *United States*, *supra*.

The district court's reliance (R. 26) upon cases such as *United States* v. *Bess*, 357 U.S. 51, was misplaced. *Bess* held only that the proceeds of life in-

surance policies (unlike their cash surrender value) were not property of the insured during his lifetime to which federal income tax liens attached; and that the transferee liability of the beneficiaries for the insured's income taxes, therefore, was limited to the cash surrender value at the time of the insured's death. The holding did not relate to estate taxes (cf. *Detroit Bank* v. *United States*, 317 U.S. 329), and there was no question of constitutionality there, or in the companion case of *Commissioner* v. *Stern*, 357 U.S. 39. The fact that the proceeds of the policies are not property of the insured during his lifetime within the meaning of the income tax lien statue does not mean that Congress could not constitutionally impose an estate tax on that portion of the proceeds for which the insured paid the premiums. See *supra*, pp. 10–14.

2. Further support for the constitutionality of the instant tax may be found in the cases sustaining the application of the estate tax to *inter vivos* transfers made in contemplation of, or intended to take effect at, death. *Milliken* v. *United States*, 283 U.S. 15; *United States* v. *Wells*, 283 U.S. 102; *Helvering* v. *City Bank Co.*, 296 U.S. 85; *Helvering* v. *Bullard*, 303 U.S. 297; *Helvering* v. *Hallock*, 309 U.S. 106, 111. The rationale of those decisions is that even though the transfer was completed during the donor's lifetime, the gift was nonetheless a means of carrying out the donor's testamentary design; Congress, therefore, was justified in treating it, for estate tax purposes, as the equivalent of a testamentary

disposition. Thus, in *Milliken* v. *United States, supra*, this Court, in upholding the constitutionality of an estate tax upon transfers in contemplation of death, stated (283 U.S. at p. 23):

> It is sufficient for present purposes, that such gifts are motivated by the same considerations as lead to testamentary dispositions of property, and made as substitutes for such dispositions without awaiting death, when transfers by will or inheritance become effective. Underlying the present statute is the policy of taxing such gifts equally with testamentary dispositions, for which they may be substituted, and the prevention of the evasion of estate taxes by gifts made before, but in contemplation of, death. It is thus an enactment in aid of, and an integral part of, the legislative scheme of taxation of transfers at death. * * *

The Court also rejected the contention that, as applied to gifts in contemplation of death that had been made when the prior Revenue Act was in force, the tax was not "one on privileges" but rather "an unapportioned direct tax" (p. 24). The Court held (*ibid.*) that since the tax was "an appropriate and indeed necessary measure to secure the effective administration of a system of death taxes, [it] is to be supported as an incident and in aid of the exercise of the constitutional power to levy a tax on the transfer of the decedent's estate at death."

Life insurance is similarly "inherently testamentary in character. * * * The acquisition of life-insurance policies on one's own life is a substitute

for a testamentary disposition of property * * *" (*Bailey* v. *United States*, 27 F. Supp. 617, 621 (Ct. Claims), rehearings granted, 30 F. Supp. 184, 31 F. Supp. 778, certiorari dismissed on stipulation, 311 U.S. 721; see also *Chase Nat. Bank* v. *United States*, 116 F. 2d 625, 627 (C.A. 2). Moreover, "An absolute assignment of such a policy even where as here there is no possibility of reverter to the assured, does not destroy the essential testamentary quality of the transaction. * * * [T]he [cash surrender] value thus acquired is substantially less than the amount of the policy payable in cash upon the death of the assured. And this residuum of value, like the value of a testamentary disposition, accrues only at the death of the assured" (*Colonial Trust Co.* v. *Kraemer*, 63 F. Supp. 866, 873 (D. Conn.))

Since the passage of the insurance proceeds in question involves "the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another" (*Chase Nat. Bank* v. *United States*, 278 U.S. 327, 337), the transfer is basically no different from the other testamentary dispositions that have been held within the scope of Congressional power to impose excise taxes. See *supra*, p. 16. Indeed, insurance proceeds present an even stronger case for the constitutionality of applying the estate tax than gifts in contemplation of death. For in the latter case, the donee receives the full measure of the property given during the donor's life, and death in no way increases the donee's interest. In the case of insurance, how-

ever, it is the death of the insured that matures the beneficiary's rights to the death proceeds.[4]

The provisions in Section 811(c) of the 1939 Code governing transfers in contemplation of, or intended to take effect in possession or enjoyment after death, and the provisions in Section 811(g) governing insurance proceeds, may fairly be viewed as reflecting the single broad purpose of subjecting to the estate tax the major substitutes for direct testamentary dispositions. A transfer "in contemplation of" death is treated as a substitute for a testamentary disposition because the thought of death motivates the transfer. A transfer "intended to take effect in possession or enjoyment at or after" the decedent's death is treated as a substitute for a testamentary disposition because of its inherent nature. By the same reasoning, the purchase of life insurance, payable at death to the insured's beneficiaries, must also be viewed as a sub-

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[4] It has been suggested in cases such as *Reinecke* v. *Northern Trust Co.*, 278 U.S. 339, 348; *Chase Nat. Bank* v. *United States*, *supra*, 278 U.S. 327, 338; and *Fernandez* v. *Wiener*, 326 U.S. 340, 362-363, that gifts made by the donor during his lifetime, not in contemplation of death, can be included in his gross estate for estate tax purposes only where some interest in or control over the property passed from him at death. However, that is not this case. For, as pointed out in the text, life insurance is sufficiently akin to testamentary dispositions to justify treating insurance proceeds as part of the insured's gross estate. While the *Chase* case dealt with estate taxation of insurance proceeds, the Court did not there consider whether such proceeds could be constitutionally taxed upon the basis of the payment of premiums by the insured. See 1 Paul, *Federal Estate and Gift Taxation* (1942 ed.), § 10.15; Lowndes and Kramer, *Federal Estate and Gift Taxes* (1956), ch. 12, Sec. 6.

stitute for a testamentary disposition. The constitutional power of Congress to treat such life insurance as part of the taxable estate certainly is no less comprehensive than its acknowledged and long recognized power to do so with respect to other classes of substitutes for testamentary dispositions, in which the decedent has parted with some or all of his interest in the transferred property prior to death.[5] Passing

[5] We do not read *Lewellyn* v. *Frick*, 268 U.S. 238, as indicating that the estate tax cannot be constitutionally applied to reach insurance proceeds for which the insured paid the premiums but with respect to which he retained no incidents of ownership in the policies. There the decedent (Frick) had taken out and assigned policies to the beneficiaries prior to the effective date of the Revenue Act of 1918; he paid all the premiums. The Collector included the entire proceeds of the policies in the gross estate, and the tax was challenged as unconstitutional. This Court, although stating (p. 251) that "there would be a very serious question to be answered" before the beneficiaries "could be made to pay a tax on the transfer of his estate by Mr. Frick" or if "it was proposed to make the estate pay a transfer tax for property that Mr. Frick did not transfer," found it unnecessary to reach the constitutional issues, for it construed the statute as applying only to transactions taking place after its passage. This holding that the Act was not applicable to transactions antedating its effective date was followed in *Bingham* v. *United States*, 296 U.S. 211, and *Industrial Trust Co.* v. *United States*, 296 U.S. 220 (involving the Revenue Act of 1926).

These cases thus hold only that the estate tax provisions of the Internal Revenue laws as they existed prior to the 1942 amendments did not purport to cover the proceeds of policies taken out before the law was passed, where the insured retained none of the incidents of ownership. The instant case, however, involves a specific statutory provision which applies the tax to the proceeds of insurance on which premiums were paid by the decedent after January 10, 1941, even though prior thereto he had disposed of all incidents of ownership in the policies.

upon the precise question here presented, the Second Circuit has held that "section 811(g)(2)(A) is a reasonable measure for Congress to take in order to prevent avoidance of the estate tax by an inter vivos transfer of life insurance where the insured has paid one or more of the premiums on such insurance." *Estate of Clarence H. Loeb*, 29 T.C. 22, 30, affirmed on the opinion of the Tax Court, 261 F. 2d 232 (C.A. 2).

B. As applied in the instant case, Section 811(g)(2)(A) does not offend the due process clause of the Fifth Amendment.

Taxpayer also contended below (R. 22) that Section 811(g)(2)(A), as amended in 1942, is "retroactive and discriminatory in its operation," in violation of the due process clause of the Fifth Amendment, when applied to the proceeds of policies that the insured had assigned prior to the effective date of the amendment. Although the court below did not refer to this argument in its brief opinion (R. 24–26), a similar argument was accepted in *Kohl* v. *United States*, 226 F. 2d 381 (C.A. 7), the "reasoning" of which case the court below accepted "as our own" (R. 26). We submit, however, that as applied in this case, Section 811(g)(2)(A) does not offend the due process clause of the Fifth Amendment.

1. The tax was not applied retroactively. Although the insured assigned all the policies to his wife in 1936, prior to the effective date of the 1942 amendment imposing the tax, he continued to pay the premiums thereon until his death in 1954. The tax

was applied only to that portion of the proceeds that was attributable to premiums that he paid after January 10, 1941, the effective date of the Treasury Regulation which subjected insurance proceeds to the estate tax on the basis of premiums paid by the decedent. See *supra*, pp. 9–10.[6] With respect to premiums paid after that date, the decedent was on notice that the insurance attributable thereto would be included as part of his gross estate for tax purposes. Cf. *Welch* v. *Henry*, 305 U.S. 134, 147; *Milliken* v. *United States, supra*, 283 U.S. at p. 24; *Estate of Clarence H. Loeb*, 29 T.C. 22, 31, affirmed, 261 F. 2d 232 (C.A. 2). Moreover, since, as we have shown (*supra*, pp. 11–14), the tax was imposed upon the ripening of the beneficiary's interest in the proceeds—long after 1942—the tax cannot be said to have been retroactively applied in any realistic sense. *United States* v. *Jacobs*, 306 U.S. 363, 366–367; *Fernandez* v. *Wiener, supra*, 326 U.S. at pp. 354–355.

In the *Jacobs* case, *supra*, the Court sustained the constitutionality of the application of the estate tax to include in the gross estate the entire value of real property paid for by the decedent but owned by him and his wife as joint tenants. The joint tenancy had been created in 1909, upon the acquisition of the property, and the tax was imposed by the Revenue Act of 1924, passed shortly before the decedent died. The taxpayer contended that to apply the tax to the

[6] Indeed, most of the premiums were paid after the 1942 amendment of the statute, which incorporated the premium-payment test of the Regulation.

entire value of the joint estate would involve retroactive taxation in violation of the Fifth Amendment. "The reasoning is that a one-half interest in the joint property was transferred to, and vested in, the wife in 1909; that the tax in question only applies to transfers; and that the one-half interest transferred to the wife in 1909 could not thereafter (1924) be taxed as a part of decedent's gross estate without retroactively applying the tax to the 1909 transfer" (p. 366).

The Court, however, held that the tax was not retroactive. It stated (pp. 366–367):

> But the tax was not levied on the 1909 transfer and was not retroactive. At decedent's death in 1924, ownership and beneficial rights in the property which had existed in both tenants jointly changed into the single ownership of the survivor. This change in ownership, attributable to the special character of joint tenancies, was made the occasion for an excise, to be measured by the value of the property in which the change of ownership occurred. Had the tenancy not been created, this survivorship and change of ownership would not have taken place, but the tax does not operate retroactively merely because some of the facts or conditions upon which its application depends came into being prior to the enactment of the tax.

By the same reasoning, the tax here was not retroactively applied. It was not levied on the 1936 assignment of the policies, but on the "change in owner-

ship" of the proceeds from the insurance company to the beneficiary, resulting from the insured's death. "[T]he tax does not operate retroactively merely because some of the facts or conditions upon which its application depends came into being prior to the enactment of the tax." *Jacobs, supra.*[7]

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[7] The contrary holding in *Kohl* rested upon a mistaken concept of the basis upon which the estate tax was applied to the proceeds of insurance for which the decedent paid the premiums—the same error committed by the district court in the instant case. See *supra*, pp. 10–11. The policies in *Kohl*, which had been issued in 1921 and 1922, were assigned on January 21, 1941, 11 days after issuance of the Treasury Regulation taxing insurance proceeds on the basis of premiums paid by the decedent, but prior to the enactment of the 1942 Act which made that test part of the Internal Revenue Code. The insured paid all premiums prior to assignment, but thereafter they were paid by the assignees. The decedent died in 1943, and the Commissioner included, as part of the gross estate, that portion of the proceeds attributable to premiums paid by the insured prior to the assignment.

In holding that the statute was applied retroactively, the court of appeals stated (226 F. 2d at p. 385) that Section 811(g), as it existed prior to the 1942 amendments, only taxed insurance received by the executor or other beneficiaries, and not "completed transfers to third persons;" that since the Treasury Regulation attempted to include the proceeds of policies that had been completely transferred to assignees, it "transcended the statute" and was "illegal and void"; and that to subject the insured's estate to "a tax on policies of which he had completely divested himself * * * [imposed] by a new statute, is to attempt to tax retroactively something not his and something upon which, at the time he gave it away, he had paid a federal tax," i.e., a gift tax.

The holding of retroactivity, therefore, rested upon the erroneous view that because the insured had divested himself of all incidents of ownership in the policies, the estate tax can-

2. The tax is neither unreasonable nor arbitrary. As we have shown (*supra*, pp. 10–15), the death of the insured "has brought into being or ripened for the [beneficiary], property rights of such character as to make appropriate the imposition of a tax upon that result" (*Tyler* v. *United States*, 281 U.S. 497, 503). And the property thus brought into being was "procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another" (*Chase Nat. Bank* v. *United States*, 278 U.S. 327). Moreover, insurance is sufficiently "akin to testamentary dispositions" (*Helvering* v. *Hallock*, 309 U.S. 106, 112) to justify Congress in treating the proceeds thereof as part of the decedent's gross estate (see *supra*, pp. 16–20). The tax fairly reflects the extent to which the decedent is responsible for creating the fund, since it is limited to that portion of the proceeds attributable to the premiums that he paid. There is nothing arbitrary in applying the tax to the proceeds even though the insured had assigned the policies prior to 1941, since only those premiums that he paid after that date are reflected in the tax.

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not be imposed upon the transfer of the proceeds to the beneficiary upon the insured's death. See discussion *supra*, pp. 10–20; *Estate of Clarence H. Loeb*, 29 T.C. 22, affirmed per T.C. 776 (in both of which the court declined to follow *Kohl*); *Colonial Trust Co.* v. *Kraemer*, 63 F. Supp. 866 (D. Conn.); *Schwarz* v. *United States*, 170 F. Supp. 2 (E.D. La.). Furthermore, *Kohl* is distinguishable in that there the premiums were paid by the decedent prior to January 10, 1941, whereas here they were paid afterwards.

curiam, 261 F. 2d 232 (C.A. 2), and Estate of Ellis Baker, 30

In sum, the tax as applied in this case does not violate the Fifth Amendment in any respect. Cf. *Burnet* v. *Wells*, 289 U.S. 670.[8]

CONCLUSION

The judgment of the District Court should be reversed.

Respectfully submitted.

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Charles K. Rice,
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January 1960.

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[8] The premium-payment test was eliminated in Section 2042 of the Internal Revenue Code of 1954, 26 U.S.C. 2042; but that change operates prospectively only with respect to estates of decedents dying after August 16, 1954.

APPENDIX

Constitution of the United States:

ARTICLE I

SECTION 2. * * *

Representatives and direct Taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers, * * *.

*   *   *   *   *

SECTION 8. The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States;

*   *   *   *   *

SECTION 9. * * *

No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken.

*   *   *   *   *

FIFTH AMENDMENT

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life,

liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

Internal Revenue Code of 1939:

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * *

(g) [as amended by Sec. 404(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Proceeds of Life Insurance.*—

(1) *Receivable by the executor.*—To the extent of the amount receivable by the executor as insurance under policies upon the life of the decedent.

(2) *Receivable by other beneficiaries.*—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance, or (B) with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person. For the purposes of clause (A) of this paragraph, if the decedent transferred, by assignment or otherwise, a policy of insurance, the amount paid directly or indirectly by the decedent shall be reduced by an amount which bears the same ratio to the amount paid directly or indirectly by the decedent as the consideration in money or money's worth received by the decedent for the transfer bears to the value of the policy at the

time of the transfer. For the purposes of clause (B) of this paragraph, the term "incident of ownership" does not include a reversionary interest.

* * * * *

(26 U.S.C. 1952 ed., Sec. 811.)

Revenue Act of 1942, c. 619, 56 Stat. 798:

SEC. 404. PROCEEDS OF LIFE INSURANCE.

* * * * *

(c) *Decedents to Which Amendments Applicable.*—The amendments made by subsection (a) shall be applicable only to estates of decedents dying after the date of the enactment of this Act [October 21, 1942]; but in determining the proportion of the premiums or other consideration paid directly or indirectly by the decedent (but not the total premiums paid) the amount so paid by the decedent on or before January 10, 1941, shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policy.

Treasury Regulations 105, promulgated under the Internal Revenue Code of 1939:

SEC. 81.27 [as amended by T.D. 5239, 1943 Cum. Bull. 1081, 1092]. *Insurance Receivable by Other Beneficiaries.*—(a) *In case of decedent dying after October 21, 1942.*—The regulations prescribed under this subsection (except as otherwise indicated herein or in subsection (b) of this section) are applicable only in the case of decedents who died after October 21, 1942, the date of the enactment of the Revenue Act of 1942. In such cases, the amount of the aggregate proceeds of all insurance on the life of the decedent not receivable by or for the benefit of his estate must also be included in his gross estate, as follows:

(1) Such insurance (not includible under (2) of this subsection) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in the proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance, and

(2) Such insurance with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any person.

* * * * *

For the purposes of (1) of this subsection, in determining the proportion of the premiums or other consideration paid directly or indirectly by the decedent (but not the total premiums paid) the amount so paid by the decedent on or before January 10, 1941, shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policy. * * *

* * * * *

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BRIEF FOR MANUFACTURERS

NATIONAL BANK OF

DETROIT, APPELLEE

FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

No. 350

UNITED STATES OF AMERICA,
Appellant,
vs.
MANUFACTURERS NATIONAL BANK OF DETROIT,
Appellee

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MICHIGAN

BRIEF FOR MANUFACTURERS NATIONAL BANK OF DETROIT, APPELLEE

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BRIEF FOR MANUFACTURERS NATIONAL BANK OF DETROIT, APPELLEE

QUESTION PRESENTED

Appellee believes that a more correct statement of the question presented is as follows:

Section 811(g)(2)(A) of the 1939 Internal Revenue Code requires inclusion in the decedent's gross estate, for purposes of the federal estate tax, of proceeds of insurance

on the life of the decedent to the extent the insurance was purchased with premiums paid by him regardless of whether he retained any incidents of ownership of the insurance policy.

The question presented is whether this provision when applied to the assets of the estate of decedent received by the executor of his will (not, as stated by the Solicitor General, to the proceeds of the policies of insurance on his life which he had assigned to the beneficiary) is unconstitutional either (1) as an unapportioned direct tax, or (2) as contravening the due process clause of the Fifth Amendment.

FACTS

The statement of facts contained in the brief of the Solicitor General is substantially correct.

SUMMARY OF ARGUMENT

The tax involved in this case is not actually imposed upon the proceeds of the insurance policies on the life of appellee's testator but instead is imposed upon the executor of his will because under state law this executor has legal possession of the assets of the decedent's estate. The tax in question is not a tax on the transfer of these assets of the estate of decedent but instead is a tax on the executor of his estate because of its possession or ownership of these assets and is therefore a direct tax and unconstitutional because unapportioned.

Authorities which approve the inclusion in the taxable estate of a decedent of the proceeds of insurance on his life where he has retained the ownership of

such policies up to his death, are not relevant; neither are authorities which permit the inclusion in the taxable estate of a decedent of gifts made by him on contemplation of death.

ARGUMENT

I. QUESTIONS INVOLVED

Subsection 811(g)(2)(A) of the Internal Revenue Code of 1939 (Appendix p. 18) requires the inclusion in the estate of a decedent for the purposes of the federal estate tax on his estate of the proceeds of policies of insurance on the life of the decedent if he has paid the premiums for such policies, even though he possessed not one of the incidents of the ownership of such policies, such as the right to change beneficiaries, the right to surrender, the right to collect the surrender value, and so on. Appellee's testator had paid the premiums on certain policies of insurance on his life up to the date of his death (R. p. 16) but in 1936 he had divested himself completely of all of the incidents of the ownership of these policies (R. p. 16). Appellant, pursuant to this section of the Code, has exacted an estate tax from appellee on the assumption that the proceeds of these policies constitute a portion of the testator's taxable estate. In this suit, appellee seeks to recover so much of the federal estate tax on the transfer of the assets of the estate of its testator, as is so referable to the proceeds of these policies of insurance. Appellee seeks this recovery on the ground that subsection 811(g)(2)(A) is unconstitutional for two reasons:

First, because it is a direct tax unapportioned contrary to Article I, Section 2, Article I, Section 8

and Article I, Section 9, of the Constitution of the United States (Appendix p. 17) and

Second, because it deprives the executor of the estate of this decedent property without due process of law contrary to the Fifth Amendment to the Constitution of the United States (Appendix p. 17).

II. THE PROCEEDS OF THESE POLICIES FORMED NO PORTION OF THE ESTATE OF THE DECEDENT

This Court has held quite recently, and in another connection, in two cases that the proceeds of insurance on the life of a decedent form no portion of his estate. The cash surrender value of insurance on the life of a decedent does form a portion of this taxable estate if the decedent had the right, up to the time of his death, to demand it but the decedent in this case had surrendered this right, and also all other rights respecting the policies here involved many years before his death (R. p. 16). The cases above mentioned are *Commissioner of Internal Revenue v. Stern,* 357 U. S. 39 and *United States v. Bess,* 357 U. S. 51. In both of these cases the widow of a decedent had received the proceeds of insurance on his life. In both cases, the United States sought to hold her liable as a transferee for income tax deficiencies of her husband. In both cases it was held that these insurance proceeds formed no part of the taxable estate of the husband, therefore, were subject to no lien for taxes and that the wife, therefore, was not liable as transferee. In *United States v. Bess,* this Court said (pp. 55-56):

> "It would be anomalous to view as 'property' subject to lien proceeds never within the insured's reach to enjoy and which are reducible to possession by another only upon the insured's death, when his right to change the beneficiary comes to an end."

While these cases deal in part with sections of the Code other than those relating to the estate tax, they are clear authority for the proposition that the proceeds of insurance on the life of a decedent form no portion of his estate.

At this point, it will be proper to point out that this involves no actual loss of revenue and offers no loophole for evasion or avoidance of taxes. When an insured transfers the incidents of the ownership of policies of insurance on his life (without the receipt of consideration), he makes a taxable gift. Thereafter, whenever he pays a premium he makes an additional taxable gift. And it is respectfully submitted that the fact that Congress might be able to secure the same amount of revenue by some sort of excise tax on life insurance, is no good reason for upholding an unapportioned direct tax on the assets of the estate of the insured, as is shown below that is exactly what Section 811(g)(2)(A) (Appendix p. 18) does.

III. THE ESTATE TAX IS A TAX ON THE TRANSFER BECAUSE OF DEATH, OF THE ASSETS OF THE ESTATES OF DECEDENTS. THE PROCEEDS OF INSURANCE ON THE LIFE OF THIS DECEDENT DO NOT CONSTITUTE ASSETS OF THIS SORT

This case is governed by the provisions of the Internal Revenue Code of 1939. Section 810, of that Code (Appendix p. 18), provides in part as follows:

> "A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in Section 812) shall be imposed upon the transfer of the net estate of every decedent citizen or resident of the United States dying after the date of the enactment of this title * * *."

It is thus a tax upon the *transfer of the ownership* of assets because of the death of their owner. Section 811, of the Code (Appendix p. 18), provides that the value of this transfer is to be determined by including in the estate of the decedent all property, real or personal, tangible or intangible, wherever situated (except real property situated outside of the United States) to the extent of the interest therein of the decedent. Now, it is clear, as has been shown and will probably be admitted by counsel for appellant, that the proceeds of the insurance policies here involved were not included or includible among the assets constituting the estate of appellee's testator. The first clause of Section 811 of the Code specifies in general the items whose transfer is to be taxed. Later subsections provide for the taxation of the transfer of various assets in which the decedent though not the sole owner had an interest, or over which he had a power which was terminated by death. It is considered that the cessation of such an interest or the termination of such a power is the equivalent of a transfer. Sections 811(c) and 811(l) provide that the subject matter of any gifts made in contemplation of death shall also be taxed as a transfer caused by death.

Thus, section 810 levies an excise tax on transfers caused by death. Section 811 specifies the items whose transfer is caused by death. Subsection 811(g)(2)(A) (Appendix p. 18), however, is different. Its validity is now for the first time before this court. It provides that the proceeds of insurance on the life of a decedent may be included in his estate because and only because he paid the premiums on them even though he was in no sense the owner of the policies. As has been shown, the proceeds of insurance on his life form no portion of the estate of a decedent and are nonexistent during his lifetime. Thus it is not these insurance

proceeds which are taxed in this case but instead the assets actually constituting the estate of the decedent; and it is not the transfer by death of these assets that is being taxed by subsection 811(g)(2)(A) since provision for that tax, as has been shown, is made by other parts of Sections 810 and 811. It is, therefore, simply a tax on the executor because of its possession of the assets constituting the estate of the decedent and is, therefore, an unapportioned direct tax. This is discussed more fully below.

IV. PREVIOUS DECISIONS OF THIS COURT ALLOWING THE INCLUSION OF THE PROCEEDS OF LIFE INSURANCE IN THE ESTATE OF A DECEDENT ARE NOT RELEVANT

As pointed out by counsel for the United States, it has long been held that proceeds of insurance on the life of a decedent may be included in his taxable estate, where, up to the time of his death he retained the incidents of ownership, such as the right to change beneficiaries, the right to receive surrender value and so on. *Chase National Bank v. United States*, 278 U. S. 327, is perhaps the leading case on this subject and has been misconstrued, it is submitted, by many of the courts, particularly by the Tax Court in *Estate of Clarence H. Loeb*, 29 T. C. 22, affirmed on the opinion of the Tax Court by the Circuit Court of Appeals for the Second Circuit 261 Fed. (2d) 232. In the Chase case, the executor of the estate of a decedent who had taken out policies of insurance on his life in favor of his wife claimed that the proceeds of these policies should not be included in his estate for the purposes of the estate tax. It was argued that the tax on these proceeds was not an excise or privilege tax but instead was a direct tax not apportioned. The decedent had retained all of the incidents of the ownership of these policies: up to the time of

his death, he could change beneficiaries, surrender the policies and so on. This court held that the proceeds of such policies could be included in the estate of the decedent for estate tax purposes, and explained carefully the reason for this holding. After pointing out that the decedent, up to the moment of his death, had retained the power to dispose of the policies and of their proceeds as completely as if he himself were the beneficiary, the court said:

> "The precise question presented is whether the termination at death of that power and the consequent passing to the designated beneficiaries of all rights under the policies freed of the possibility of its exercise may be the legitimate subject of a transfer tax, as is true of the termination by death of any of the other legal incidents of property through which its use or economic enjoyment may be controlled" (pp. 334-335).

and later

> "As it is the termination of the power of disposition of the policies by decedent at death which operates as an effective transfer and is subjected to the tax, there can be no objection to measuring the tax or fixing its rate by including in the gross estate the value of the policies at the time of death, together with the other interests of decedent transferred at his death" (p. 339).

In the case at bar, no power of disposition terminated at the death of appellee's testator, the policies had all been surrendered by him many years ago. Far from being an authority that the proceeds of the policies involved in this case may be included in the gross estate of the decedent for estate tax purposes, the Chase case is an authority that they may not be so included. The Chase case simply holds that where death terminates a power of control which a

decedent has over an asset, the value of that asset may be included in his estate for estate tax purposes. This court is now being asked to hold that, even though no right or power which the decedent possessed with respect to these policies is terminated or even remotely affected by his death, still the proceeds of these policies (an asset which was not in existence till after his death) may be used as the measure of a tax upon his executor as possessor of the assets constituting his estate, not because of the transfer of those assets, but solely because they are in the possession of the executor.

The same principle was stated in *Fernandez v. Wiener*, 326 U. S. 340. There the decedent was a resident of a state in which the law as to the community property of husband and wife was in effect. The total face value of policies of insurance on his life, bought with community funds, was included in his estate for purposes of the estate tax. The decedent had retained the right to change the beneficiaries of these policies. In holding that the total proceeds of these policies could be included in the taxable estate of the decedent this court said:

> "For reasons which we have already fully developed in this opinion, the death of the insured, since it ended his control over the disposition of the proceeds and gave his wife the present enjoyment of them, may be constitutionally made the occasion for the imposition of an indirect tax measured by the proceeds themselves" (p. 363).

What made the proceeds of these policies includible in the estate of the decedent for estate tax purposes was the fact that he had retained until he died the incidents of the ownership of the policies.

If the decedent in the present case had continued to possess the incidents of the ownership of these policies till he died, they would have been includible in his estate for tax purposes. But now this court is asked to sanction something entirely different: it is asked to sanction a tax (not a transfer tax) upon the assets actually comprised in his estate because he paid the premiums on these policies even though neither these policies nor their proceeds were among the assets of his estate.

V. GIFTS IN CONTEMPLATION OF DEATH

In its brief, the appellant has laid considerable stress on the fact that the value of a gift made in contemplation of death may, upon the death of the donor, be included among the assets of his estate for the purposes of the estate tax. Apparently it argues that because this is permissible, it is also permissible to include in the estate of a decedent, the proceeds of policies of insurance on his life, though he had no interest in and no power over the policies or their proceeds, because and only because he paid the premiums for them. The distinction between gifts *mortis causa* and insurance of this type is, of course, obvious. In every gift in contemplation of death there is by hypothesis a *transfer* of some *res "mortis causa"*—"because of death." This is clearly shown in the concluding sentences of *Milliken v. United States*, 283 U. S. 15 (cited at page 15 of the appellant's brief) where the court says (pp. 24-25):

> "* * * we think the present tax is to be supported as an incident and in aid of the exercise of the constitutional power to levy a tax on *the transfer of the decedent's estate at death.*" (Emphasis supplied.)

The tax involved in that case was an estate tax on a gift *mortis causa.*

Clearly, there was no transfer of the insurance proceeds involved in the present case, either from the decedent or from his estate. Neither those proceeds nor the right to receive them came into existence until after he had died. But appellant argues, we understand, somewhat as follows: The inclusion of gifts *mortis causa* in the estate of the donor is desirable for the purpose of preventing undue avoidance of estate taxes. For the same reason, the inclusion in the taxable estate of a decedent of the proceeds of policies of insurance on his life, because and only because he has paid the premiums for them, would likewise be desirable for the same reason. Perhaps so, but this does not prove that it is constitutionally permissible to obtain this result, by means of an unapportioned direct tax on the assets which actually constitute his estate. Nor is it relevant that the same result could be obtained and the same amount of tax revenue exacted by some sort of constitutional excise tax. This would probably be possible in the case of any direct tax that might be levied without apportionment by the United States: some excise tax could be thought of which would exact the same amount of money.[1]

Incidentally, it is to be noted that Congress does not feel that failure to exact this tax will result in any serious tax avoidance, since under the Internal Revenue Code of 1954 (Section 2042, Appendix p. 20) there is no attempt to tax the estate of a decedent because of policies of insurance on his life which he did not own but for which he paid

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[1] This is neatly illustrated by the recent cases of *Railway Express Agency v. Virginia*, 347 U. S. 359, and *Railway Express Agency v. Virginia*, 358 U. S. 434. In these cases a franchise tax which infringed the Commerce Clause of the Constitution was rendered valid when it was designated as a tax in lieu of all other taxes on intangible personal property.

the premiums. Or possibly Congress has recognized that an attempt so to tax them would be unconstitutional.

VI. IN THIS CASE A NEW QUESTION IS PRESENTED TO THIS COURT

As has been stated, there are various other situations in which it has been held that the terminatian of some power or interest possessed by a decedent with respect to some asset permits its inclusion in his estate for estate tax purposes: for example, the corpus of a trust created by him where he has reserved to himself for his lifetime the income from the trust. But always there is some valuable asset existing during the lifetime of the decedent as to which he has during his lifetime some power or interest which is extinguished by his death. This decedent had no power or interest whatsoever with respect to the insurance premiums here involved. To include these proceeds in his taxable estate borders on the absurd. Suppose a man's wife is killed by the actionable negligence of a third party and that in the jurisdiction where she was killed and where the husband is domiciled he has a right to recover damages for loss of her services. It would be as sensible to include this right to recover damages which the husband has, among the assets of her taxable estate, as to include these insurance proceeds in the estate of this decedent.

It is significant that Congress and the Bureau of Internal Revenue (now the "Internal Revenue Service") have constantly, over the years, altered their treatment of this matter, that is, the inclusion of the proceeds of insurance on the life of a decedent in his estate at death because, and only because, he has paid the premiums for that insurance. Sometimes such policies have been held to be includible—sometimes not, and there has been a great deal of doubt

and confusion. The policies here involved were assigned to the wife, now widow of decedent, on December 15, 1936 (R. p. 16). Shortly thereafter, on March 3, 1937, T. D. 4729 (Cum. Bul. 1937-1, p. 284) was approved. Under this T. D. the policies would not have been included in his estate even though he paid the premiums for them. On January 10, 1941, T. D. 5032 (Cum. Bul. 1941-1 p. 427) was approved, in substance it reversed T. D. 4729 and reinstated the payment of premiums test. The Revenue Act of 1942 enacted in substance of this T. D. and, as amended, was still in effect on July 15, 1954, the date of the death of appellee's testator. The Internal Revenue Code of 1954 became effective thirty-two days later on August 16, 1954, and this Code omits the payment of premium test for the inclusion of life insurance (Section 2042). Appendix p. 20).

VII. IT IS IMMATERIAL THAT THE EXECUTOR IS GIVEN A RIGHT OF RECOVERY AGAINST THE RECIPIENT OF THE PROCEEDS OF THESE POLICIES

It is true that the executor is given a right of recovery of a portion of the estate tax paid by it from the recipient of the insurance proceeds (Internal Revenue Code 1939, Section 826(c) (Appendix p. 19)), but this is wholly immaterial. Section 822(b) of the 1939 Code (Appendix p. 19) is as follows:

> "The tax imposed by this subchapter shall be paid by the executor to the collector."

If the beneficiary of the life insurance dissipates the proceeds and becomes penniless before the executor can sue him, that is wholly immaterial. No portion of the tax paid will be returned to the executor and the executor is liable

for the tax because and solely because it is the entity to which the state law gives possession of the assets of the decedent. It is liable for the payment of this tax because it has possession of such assets and the tax referable to the insurance proceeds is not a tax on the transfer of these other assets for that transfer is taxed by other sections of the Code as has been stated.

VIII. THE TAX IS, THEREFORE, A DIRECT TAX AND UNCONSTITUTIONAL BECAUSE NOT APPORTIONED

It is elementary that a tax on property is a direct tax and that to levy a tax by reason of the ownership or possession of property, is to tax property. *Pollock v. Farmers Loan and Trust Company*, 157 U. S. 429, and on rehearing 158 U. S. 601. *Dawson v. Kentucky Distillers and Warehouse Co.*, 255 U. S. 288. In that case, this court said:

> "To levy a tax by reason of the ownership of property is to tax property" (p. 294).

Bromley v. McCaughn, 280 U. S. 124. In its opinion in that case, the Court stated:

> "While taxes levied or collected from persons because of their general ownership of property may be direct" (citing the Pollock case) "this court has consistently held, almost from the foundation of the government that a tax imposed upon a particular use of property or the exercise of a single power over property incidental to ownership is an excise tax which need not be apportioned, * * *" (p. 136).

In the dissenting opinion in the same case, Justice Sutherland said:

> "Since the Pollock case however we know that a tax on property, whether real or personal or upon

> the income derived therefrom is direct, and that to levy a tax by reason of the ownership of property is to tax property" (pp. 139-140).

Now, very clearly, as stated, the tax here involved is levied against the executor because of its possession of the assets of the decedent and the proceeds of these policies, as has been shown, form no part of his estate and neither the decedent nor the executor has in any way used or has in any way exercised a power over these insurance proceeds. The executor is liable for the tax because and solely because it is the entity to which state law gives possession of the assets of the decedent, and it is liable for the payment of this tax because it has possession of such assets. This is, therefore, a direct tax and unconstitutional because not apportioned.

IX. DUE PROCESS

The appellant has argued in substance (Brief, pp. 22-25) that the tax is not retroactive and there is no denial of due process under the Fifth Amendment because allowance was made for any premiums on the insurance paid by the decedent prior to the change in the law which included the proceeds of insurance policies in his taxable estate because and solely because he paid the premiums for them. But this is not enough. Before the enactment of the Act of 1942 and in reliance on the law as it had been, the petitioner had parted irrevocably with all ownership of and all power over the policies involved. He could not take them back. He had the choice of only two courses of action: he could stop paying the premiums—in which case the policies would be destroyed; or, he could continue paying premiums—in which case they would be included in his estate, but that is all that he could do.

CONCLUSION

It is respectfully submitted that the judgment of the District Court should be affirmed.

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APPENDIX

Constitution of the United States:

ARTICLE I

Section 2. * * *

Representatives and direct Taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers, * * *.

* * * * *

Section 8. The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defense and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States;

* * * * *

Section 9. * * *

No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken.

* * * * *

FIFTH AMENDMENT

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of

life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

Internal Revenue Code of 1939:

Sec. 810. Rate of Tax.

A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 812) shall be imposed upon the transfer of the net estate of every decedent, citizen or resident of the United States, dying after the date of the enactment of this title.

* * * * *

Sec. 811. Gross Estate.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * *

(g) [as amended by Sec. 404(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Proceeds of Life Insurance.*

(1) *Receivable by the executor.*—To the extent of the amount receivable by the executor as insurance under policies upon the life of the decedent.

(2) *Receivable by other beneficiaries.*—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in proportion that the

amount so paid by the decedent bears to the total premiums paid for the insurance, or (B) with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person. For the purposes of clause (A) of this paragraph, if the decedent transferred, by assignment or otherwise, a policy of insurance, the amount paid directly or indirectly by the decedent shall be reduced by an amount which bears the same ratio to the amount paid directly or indirectly by the decedent as the consideration in money or money's worth received by the decedent for the transfer bears to the value of the policy at the time of the transfer. For the purposes of clause (B) of this paragraph, the term "incident of ownership" does not include a reversionary interest.

* * * * *

Sec. 822(b) Liability for Payment.

The tax imposed by this subchapter shall be paid by the executor to the collector.

Sec. 826(c). Liability of Life Insurance Beneficiaries.

Unless the decedent directs otherwise in his will, if any part of the gross estate upon which tax has been paid consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds of such policies bear to the sum of the net estate and the amount of the exemption allowed in computing the net estate, determined under section 935 (c). If there is more than one such benficiary the executor shall be entitled to recover from such beneficiaries in the same ratio. In the case of such proceeds receivable by the surviving spouse

of the decedent for which a deduction is allowed under section 812(e) (the so-called "marital deduction"), this subsection shall not apply to such proceeds except as to the amount thereof in excess of the aggregate amount of the marital deductions allowed under such subsection.

Internal Revenue Code of 1954:

Sec. 2042. Proceeds of Life Insurance.

The value of the gross estate shall include the value of all property—

(1) Receivable by the Executor.—To the extent of the amount receivable by the executor as insurance under policies on the life of the decedent.

(2) Receivable by Other Beneficiaries.—To the extent of the amount receivable by all other beneficiaries as insurance under policies on the life of the decedent with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person. For purposes of the preceding sentence, the term "incident of ownership" includes a reversionary interest (whether arising by the express terms of the policy or other instrument or by operation of law) only if the value of such reversionary interest exceeded 5 percent of the value of the policy immediately before the death of the decedent. As used in this paragraph, the term "reversionary interest" includes a possibility that the policy, or the proceeds of the policy, may return to the decedent or his estate, or may be subject to a power of disposition by him. The value of a reversionary interest at any time shall be determined (without regard to the fact of the decedent's death) by usual methods of valuation, including the use of tables of mor-

tality and actuarial principles, pursuant to regulations prescribed by the Secretary or his delegate. In determining the value of a possibility that the policy or proceeds thereof may be subject to a power of disposition by the decedent, such possibility shall be valued as if it were a possibility that such policy or proceeds may return to the decedent or his estate.

POLICY FOR
THE
UNITED STATES

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FILED

In the Supreme Court of the United States

OCTOBER TERM, 1959

No. 350

UNITED STATES OF AMERICA, APPELLANT,

v.

MANUFACTURERS NATIONAL BANK OF DETROIT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MICHIGAN

REPLY BRIEF FOR THE UNITED STATES

1. Appellee cites (Br. 4-5) *Commissioner* v. *Stern*, 357 U.S. 39, and *United States* v. *Bess*, 357 U.S. 51, as authority for the proposition that the proceeds of insurance on the life of a decedent form no portion of his taxable estate. But the cases do not so hold and, as pointed out in our main brief (pp. 14-15), they have no bearing on estate taxes at all. Indeed, if they so held, they would be contrary to *Chase Nat. Bank* v. *United States*, 278 U.S. 327, for the decedents in *Stern* and *Bess* both retained incidents of ownership in their policies until they died, as did the decedent in the *Chase Nat. Bank* case. The insurance

proceeds in the *Chase* case, however, were held to be part of the decedent's estate. Moreover, *Stern* and *Bess* recognized (see *Commissioner* v. *Stern*, 357 U.S. at p. 43, fn. 3) that the income tax transferee provisions are different from the estate tax transferee provisions. The latter do treat life insurance proceeds, to the extent includable in the decedent's gross estate under Section 811(g) of the 1939 Code, as property of the decedent. See *Commissioner* v. *Chase Manhattan Bank*, 259 F. 2d 231, 256 (C.A. 5), certiorari denied, 359 U.S. 913.

It is true, as appellee states (Br. 5), that when an insured transfers the ownership of a policy on his life to another he makes a taxable gift; and if he thereafter pays a premium he makes an additional taxable gift. *Guggenheim* v. *Rasquin*, 312 U.S. 254; *Powers* v. *Commissioner*, 312 U.S. 259; *United States* v. *Ryerson*, 312 U.S. 260; *Commissioner* v. *Berger*, 201 F. 2d 171 (C.A. 2); Treasury Regulations 108, Section 86.2 (a)(8).[1] But that does not prove that the portion of

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[1] Section 86.2(a)(8) provides as follows:

> If the insured purchases a life insurance policy, or pays a premium on a previously issued policy, the proceeds of which are payable to a beneficiary or beneficiaries other than his estate, and with respect to which the insured retains no power to revest the economic benefits in himself or his estate or to change the beneficiaries or their proportionate benefits (or if the insured relinquishes by assignment, by designation of a new beneficiary or otherwise, every such power that was retained in a previously issued policy), the insured consummates a gift of the value of such policy, or to the extent of such premium, even though the right of the assignee or beneficiary to receive the benefits is conditioned upon his surviving the insured * * *

the proceeds for which he has paid the premiums may not constitutionally be included as part of his gross estate; it indicates only that the estate may be entitled to an appropriate credit on the estate tax for any gift taxes paid. *Smith* v. *Shaughnessy*, 318 U.S. 176, 179; Internal Revenue Code of 1939, Section 813(a). In the instant case, however, it has not been shown that any such gift taxes were paid.

2. Appellee states (Br. 6) that the estate tax is imposed upon the transfer of the ownership of assets because of the death of their owner. But, as pointed out in our main brief (pp. 15-16, for example), it has long been settled that the estate tax extends not only to property owned by the decedent but also to property transferred by him during his lifetime where the transfers are substitutes for testamentary dispositions, such as transfers in contemplation of death. Although appellee urges (Br. 10-11) that the tax on transfers in contemplation of death is limited to gifts *causa mortis* (which are made in anticipation of impending death, are revocable, and are defeated if the donor survives the apprehended peril (*Basket* v. *Hassell*, 107 U.S. 602, 609, 610)), it has long been settled (*United States* v. *Wells*, 283 U.S. 102, 115-116) that the tax is not confined to such gifts. The statute taxing transfers in contemplation of death (Section 811(c) of the 1939 Code) embraces gifts *inter vivos*, even though they are fully executed, irrevocable and indefeasible. *United States* v. *Wells*, 283 U.S. 102, 116. Therefore, the donative premium payments made by the instant decedent support the constitutionality of a tax on the

proceeds built up by such premiums in much the same manner as a gift made in contemplation of death supports and justifies a tax on the value of the property at the time of decedent's death. *Milliken* v. *United States*, 283 U.S. 15, 23; *Central Hanover Bank Co.* v. *Kelly*, 319 U.S. 94, 97-98; *Iglehart* v. *Commissioner*, 77 F. 2d 704, 711 (C.A. 5); *Humphrey's Estate* v. *Commissioner*, 162 F. 2d 1, 2 (C.A. 5), certiorari denied, 332 U.S. 817.[2]

3. Appellee urges (Br. 15) that the instant tax is levied against the executor because state law gives the executor possession of assets owned by the decedent at the time of death. Assuming that to be so (see Internal Revenue Code of 1939, Section 822; Paul, *Federal Estate and Gift Taxation* (1942 ed.), Section 13.16), it does not follow that only property actually owned

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[2] We agree with appellee (Br. 13-14) that it is immaterial that the executor is given a right of recovery of a proportion of the estate tax paid by it from the recipient of the insurance proceeds (Section 826(c) of the Internal Revenue Code of 1939; see Appendix to appellee's brief, p. 19). Generally speaking, the intent of Congress was that the federal estate tax should be paid out of the estate as a whole, and that the distribution of the remaining estate and the ultimate impact of the federal tax should be determined under state law. The Congressional directive in Section 826(c), authorizing the executor to collect the proportionate share of the tax from the beneficiary of life insurance includable in the gross estate by reason of Section 811(g), is wholly compatible with that intention. *Riggs* v. *Del Drago*, 317 U.S. 95, 101-102. The responsibility for the payment of the federal estate tax rests upon the executor in his representative capacity and the Government looks to him for the performance of this duty. *In Re Tarver's Estate*, 255 F. 2d 913, 917 (C.A. 4). See Paul, *Federal Estate and Gift Taxation* (1946 Supp.), Section 13.54, p. 465; Lowndes and Kramer, *Federal Estate and Gift Taxes* (1956), ch. 23, Sec. 18.

by the decedent can be constitutionally subjected to the federal estate tax. On the contrary, cases such as *Tyler* v. *United States*, 281 U.S. 497 (involving tenancy by the entirety) have sustained the inclusion of property in the gross estate even though the decedent did not own it at the time of death and it did not constitute a part of his probate estate or pass to his executor.

4. Finally, appellee contends (Br. 15) that the instant tax violates due process because the decedent gave the policies to his wife prior to the enactment of the Revenue Act of 1942 and thereafter he had to choose between stopping payment of premiums, in which case the policies would be destroyed, or continuing to pay premiums, in which case a proportionate part of the proceeds would be included in his gross estate. But subjecting the decedent to such a choice [3] would not render the statute unconstitutional. To sustain its argument, appellee must show that in attributing to decedent the ownership of a portion of the proceeds of insurance and requiring the inclusion of such portion in his taxable estate, "the lawmakers have done a wholly arbitrary thing, have found equivalence where there was none or anything approaching it, and laid a burden unrelated to privilege or benefit." *Burnet* v.

[3] Obviously if decedent stopped payment of premiums the policies would not be *destroyed*; other persons—the beneficiaries—thereafter might pay premiums with their own funds, and in any event the beneficiaries would not forfeit the cash surrender values, and might even elect to obtain paid up insurance for a lesser amount or extended paid up term insurance for the face amount.

Wells, 289 U.S. 670, 679. Plainly, appellee has not made, and cannot make, such a showing.

Respectfully submitted,

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MARCH 1960.

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SUPREME COURT OF THE UNITED STATES

No. 350.—OCTOBER TERM, 1959.

United States of America, Appellant, v. Manufacturers National Bank of Detroit, etc.	On Appeal From the United States District Court for the Eastern District of Michigan.

[June 13, 1960.]

MR. CHIEF JUSTICE WARREN delivered the opinion of the Court.

The question here is whether Section 811 (g)(2)(A) of the Internal Revenue Code of 1939 is constitutional as applied in this case. That section, the "payment of premiums" provision in the 1939 Code, requires inclusion of insurance proceeds in the gross estate of an insured where the proceeds are receivable by beneficiaries other than the executor but are attributable to premiums paid by the insured.[1] Inclusion is required regardless of

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[1] These provisions were enacted, through amendment of § 811 (g), by § 404 (a) of the Revenue Act of 1942, 56 Stat. 798, 944. As amended, § 811 provides in pertinent part that:

"The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

"(g) *Proceeds of Life Insurance.*—

"(1) *Receivable by the executor.*—To the extent of the amount receivable by the executor as insurance under policies upon the life of the decedent.

"(2) *Receivable by other beneficiaries.*—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in propor-

whether the insured retained any policy rights. However, if the insured possessed no "incide[illegible]s of ownership" after January 10, 1941, the premiums paid by him before that date are excluded in determining the portion of the proceeds for which he paid the premiums.[2]

The facts in the case are stipulated. The insured died testate on July 15, 1954. The taxpayer is his executor. On the estate tax return, the taxpayer included, as part of the gross estate, the proceeds of four insurance policies payable to the wife of the insured. These policies were originally issued to the insured, but he divested himself of the policy rights by assigning them to his wife on December 18, 1936. However, he continued to pay the premiums on the policies until he died. After his death,

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tion that the amount so [illegible] by the decedent bears to the total premiums paid for the in[illegible]e, or (B) with respect to which the decedent possessed at his [illegible] any of the incidents of ownership, exercisable either alone or in conjunction with any other person.

[2] § 404 (c), Revenue Act of 1942, 56 Stat. 798, 945. Section 404 (c) provides that:

"The amendments made by subsection (a) [see note 1, *supra*] shall be applicable only to estates of decedents dying after the date of the enactment of this Act [October 21, 1942]; but in determining the proportion of the premiums or other consideration paid directly or indirectly by the decedent (but not the total premiums paid) the amount so paid by the decedent on or before January 10, 1941, shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policy."

January 10, 1941, was the effective date of a Treasury Regulation, T. D. 5032, 1941-1 Cum. Bull. 427, which provided for use of the "payment of premiums" test under § 811 (g) as it existed prior to the 1942 amendments, see note 1, *supra*, regardless of whether the decedent retained any incidents of ownership. The regulation also provided, however, that premiums paid by the decedent before its effective date were to be excluded if the decedent did not thereafter possess any incidents of ownership.

It should be noted that the "payment of premiums" test was abandoned in the 1954 Code, which reverted to the exclusive use of the "incidents of ownership" test. See 26 U. S. C. § 2042.

the proceeds were retained by the insurer for the benefit of the family, pursuant to the provisions of a settlement option selected by the wife.

In auditing the return, the Revenue Service determined that only the portion of the proceeds attributable to premiums paid by the insured after January 10, 1941, should be included in his estate.[3] Accordingly, the tax was adjusted and a refund was made. The executor then filed a claim for refund of the rest of the tax attributable to the inclusion of the proceeds. The executor claimed that because the decedent had divested himself of all interest in the policies in 1936, the tax constituted an unapportioned direct tax on property, invalid under Article I, Sections 2 and 9, of the Constitution.[4] However, the Commissioner refused to allow the claim, and the present suit for refund followed. In the District Court, the executor added a claim that the tax is also invalid under the Due Process Clause of the Fifth Amendment "because it is retroactive and discriminatory in its operation."

The District Court sustained the taxpayer's contention that, as applied in this case, Section 811 (g)(2)(A) is unconstitutional. It held that because the decedent retained no incidents of ownership in the policies after 1936, "no transfer of the property herein sought to be included in the estate of this decedent occurred at the time of his death." The court concluded that the tax was

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[3] See note 2, *supra*.

[4] Article I, § 2, provides in pertinent part that:

"Representatives and direct Taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers. . . ."

Article I, § 9, provides in pertinent part that:

"No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken."

therefore a direct tax on the proceeds themselves and could not be levied without apportionment.[5] The Government appealed directly to this Court under Sections 1252 and 2101 of Title 28, and we noted jurisdiction. 361 U. S. 880.

The first objection to the tax is that it is a direct tax—that is, that it is not a tax upon a transfer or other taxable event but is, instead, a tax upon property—which Congress cannot exact without apportionment.

This argument does not do justice to the evident intent of Congress to tax events, "as distinguished from [their] tangible fruits." *Tyler* v. *United States*, 281 U. S. 497, 502. From its inception, the estate tax has been a tax on a class of events which Congress has chosen to label, in the provision which actually imposes the tax, "the *transfer* of the net estate of every decedent."[6] See *New York Trust Co.* v. *Eisner*, 256 U. S. 345. If there is any taxable event here which can fairly be said to be a "transfer" under this language in Section 810 of the 1939 Code, the tax is clearly constitutional without apportionment. For such a tax has always "been treated as a duty or excise, because of the particular occasion which gives rise to its levy." *Knowlton* v. *Moore*, 178 U. S. 41, 81; *New York Trust Co.* v. *Eisner*, *supra*, at 349.

Under the statute, the occasion for the tax is the maturing of the beneficiaries' right to the proceeds upon the

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[5] This result is in accord with *Kohl* v. *United States*, 226 F. 2d 381 (C. A. 7th Cir.), the reasoning of which the District Court "adopted" as its own. As the District Court recognized, *Kohl* is in conflict with *Estate of Loeb* v. *Commissioner*, 261 F. 2d 232 (C. A. 2d Cir.), affirming 29 T. C. 22; *Schwarz* v. *United States*, 170 F. Supp. 2; cf. *Colonial Trust Co.* v. *Kraemer*, 63 F. Supp. 866; *Estate of Baker* v. *Commissioner*, 30 T. C. 776.

[6] Compare § 201 of the Internal Revenue Act of 1916, 39 Stat. 756, 777, with § 810 of the Internal Revenue Code of 1939, 53 Stat. 120. In the 1954 Code, the word "taxable" was substituted for the word "net" in this provision. 26 U. S. C. § 2001.

death of the insured. Of course, if the insured possessed no policy rights, there is no transfer of any interest *from him* at the moment of death. But that fact is not material, for the taxable "transfer," the maturing of the beneficiaries' right to the proceeds, is the crucial last step in what Congress can reasonably treat as a testamentary disposition by the insured in favor of the beneficiaries. That disposition, which began with the payment of premiums by the insured, is completed by his death. His death creates a genuine enlargement of the beneficiaries' rights. It is the "generating source" of the full value of the proceeds. See *Schwarz* v. *United States,* 170 F. Supp. 2, 6. The maturing of the right to proceeds is therefore an appropriate occasion for taxing the transaction to the estate of the insured. Cf. *Tyler* v. *United States,* 281 U. S. 497, 503, 504.

There is no inconsistency between such a view of the taxable event and the basic definition of the subject of the tax in Section 810. "Obviously, the word 'transfer' in the statute, or the privilege which may constitutionally be taxed, cannot be taken in such a restricted sense as to refer only to the passing of particular items of property directly from the decedent to the transferee. It must . . . at least include the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another." *Chase National Bank* v. *United States,* 278 U. S. 327, 337.

It makes no difference that the payment of premiums occurred during the lifetime of the insured and indirectly effected an *inter vivos* transfer of property to the owner of the policy rights. Congress can properly impose excise taxes on wholly *inter vivos* gifts. *Bromley* v. *McCaughn,* 280 U. S. 124. It may impose an estate tax on *inter vivos* transfers looking toward death. *Milliken* v. *United States,* 283 U. S. 15. Surely, then, it may impose such a

tax on the final step—the maturing of the right to proceeds—in a partly *inter vivos* transaction completed by death. The question is not whether there has been, in the strict sense of the word, a "transfer" of property owned by the decedent at the time of his death, but whether "the death has brought into being or ripened for the survivor, property rights of such character as to make appropriate the imposition of a tax upon that result. . . ." *Tyler* v. *United States, supra*, at 503.

Therefore, this tax, laid on the "ripening," at death, of rights paid for by the decedent, is not a direct tax within the meaning of the Constitution. Cf. *Chase National Bank* v. *United States, supra; Fernandez* v. *Wiener*, 326 U. S. 340; *Tyler* v. *United States, supra; United States* v. *Jacobs*, 306 U. S. 363.[7]

Further objections to the statute as applied in this case are predicated on the Due Process Clause of the Fifth Amendment.

It is said that the statute operates retroactively. But the taxable event—the maturing of the policies at death—occurred long after the enactment of Section 811 (g)(2)(A) in 1942. Moreover, the payment of all but a few of the premiums in question occurred after the effective date of the statute, and those few were paid during the period after January 10, 1941, when regulations gave the insured fair notice of the likely tax consequences. See T. D. 5032, 1941-1 Cum. Bull. 427.[8] Therefore, the

[7] Our view of the nature of the taxable event here involved makes it unnecessary to discuss *United States* v. *Bess*, 357 U. S. 51, and other similar cases relied on by the District Court. Nor do we find it necessary to consider at length *Lewellyn* v. *Frick*, 268 U. S. 238, or its progeny. The Court in *Frick* did not reach the constitutional issue.

[8] We do not agree with the holding in *Kohl* v. *United States*, 226 F. 2d 381, that T. D. 5032 "transcended" § 811 (g) as it existed in 1941 and that it was therefore "illegal and void." T. D. 5032, in

statute cannot be said to be retroactive in its impact. It is not material that the policies were purchased and the policy rights were assigned before the statute was enacted. The tax is not laid on the creation or transfer of the policy rights, and it "does not operate retroactively merely because some of the facts or conditions upon which its application depends came into being prior to the enactment of the tax." *United States* v. *Jacobs, supra*, at 367.

The taxpayer argues, however, that the enactment of the statute subjected the insured to a choice between unpleasant alternatives: "[H]e could stop paying the premiums—in which case the policies would be destroyed; or, he could continue paying premiums—in which case they would be included in his estate." But when he gave away the policy rights, the possibility that he would eventually be faced with that choice was an obvious risk, in view of the administrative history of the "payment of premiums" test. See 1 Paul, Federal Estate and Gift Taxation, § 10.13. The executor should not complain because his decedent gambled and lost. And, while it may be true that the insured could have avoided the tax only at the price of a loss on an investment already made, that fact alone does not prove that the lawmakers did "a wholly arbitrary thing," or that they "found equivalence where there was none," or that they "laid a burden unrelated to privilege or benefit." *Burnet* v. *Wells*, 289 U. S. 670, 679. Without such a showing, it cannot be held that the tax offends due process.

Reversed.

MR. JUSTICE DOUGLAS took no part in the consideration or decision of this case.

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effect, construed the controlling language in the earlier statute—"taken out by the decedent," 53 Stat. 122—as meaning paid for by the insured. Such a construction was clearly not unreasonable.